THE COMPETITIVENESS PROGRAM (TCP)

A Sri Lankan Case Study of Firm-Level Competitiveness

Hemas Holdings Limited

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Executive Summary

This study looks at the historic evolution of Hemas Holdings, one of Sri Lanka's most successful family owned and managed businesses, that evolved from an SME into a publicly quoted diversified group of companies that delivers some of the highest shareholder returns on the Colombo Stock Exchange. Hemas' business interests are classified under five diverse areas, namely Leisure, Transportation, Health Care, Fast Moving Consumer Goods (FMCG), and Strategic Investments.

Since its origins as a family business Hemas has always displayed a blend of entrepreneurial spirit and passion about business. The owners are known to have high standards of business ethics and are well respected for their integrity and strong capacity for marketing and building brands. The family's discipline and ability to transcend the internal bickering on ownership, typical of some family businesses, have been a cornerstone of Hemas survival and success.

Like other family businesses, Hemas too has grappled with issues such as a lack of forum for discussion and criticism of the business, a blurring of the division between business and family affairs, and difficulty in attracting and retaining professionals. Where Hemas differs is that it had the strength to address these issues by bringing in respected professionals for advice and to help with transforming the company. Furthermore, Hemas realized the need to go public and allow the marketplace to establish its true tradable worth in order to unlock the real value of the company.

Hemas' success factors

Hemas' overall success over the past five decades can be attributed largely to the following behavioral practices rooted in their approach to business.

- ***Cultural heritage***: The Esufally family's cultural heritage provides them the drive to succeed in business along with a strong discipline that prevents them from financial excesses. They live a moderate lifestyle. They are passionate about proving themselves and growing the business beyond that which their fathers bequeathed to them. The owner's truly believe in their business and communicate their sentiments, beliefs, discipline, commitment and enthusiasm to their employees in a very practical way, by working side by side with them towards common goals. The family has a very strong work ethic and expect the same of their employees.
- ***Success in building relationships.*** This refers to the ability of Hemas to build strong personal relationships with their suppliers/principals, distributors and staff. Today, this practice extends to company shareholders and financial markets analysts. A small and nimble company in the beginning, Hemas was able to bring in a personal element to its relationships on all fronts. The company built and leveraged trust as a competitive differentiator.
- ***Strong employee relations***: Employees enjoyed and relied upon Hemas paternalistic, humane approach. The Esufally family showed a genuine concern for the employees' well being, visiting their family members in hospital, providing interest free loans, and helping at times of personal crises, such as civil disturbances and/or robberies.
- ***Recruiting and empowering professionals.*** Hemas' Directors have demonstrated an aptitude for consistently identifying and recruiting capable and committed professionals, whose decisions they have generally respected and fully supported. While maintaining a clear command and control structure, they were open to input from professionals on key business issues. Most importantly, they were able to impart to all employees a genuine sense of pride for their achievements and recognized their contribution to the company's success.
- ***Understanding consumers and markets:*** The company has a strong track record of solid branding strategies and creating products which cater to consumer needs. Distribution and marketing have always been their two main strengths, while product innovation and quality were weaker. Above all, it has a commitment to spending on building new brands and creating relevant high impact advertising

campaigns. Though quality is not necessarily a passion, the company has it as a management concept.

- ***Ability to transform and innovate.*** Hemas has continuously adapted and changed with the times, opening and exiting businesses according to the prevailing business climate. Over a period of 45 years, it has gradually evolved from a small family owned core product trading business to a diversified publicly traded company that is professionally managed. Hemas has transformed its attitudes to think on a larger scale, to use expert consultants, bring in outside directors, and harness new technology.
- ***Leadership:*** The overriding present management style is defined by the "seemingly laid back but strong sense of direction" approach taken by Husein Esufally who has masterminded and made possible the recent evolution of the company. He has shown behavioral competencies that are worthy of study. Leadership is possibly the most important ingredient that needs to be built into Sri Lankan businesses. The spirit of entrepreneurship is helped by cultural environment and socio-ethnic values but it ultimately boils down to a set of characteristics that can be developed and adapted.
- ***Values:*** The company has a strong set of values which are not particularly ritualized through internal communication and Human Resource process but rather are lived through corporate style and business decisions. Hemas overriding values are integrity, strong work ethic, culture of discipline, guiding principal of simplicity, frugality, commitment, and passion about the business.
- ***Corporate Social Responsibility:*** Hemas efforts in this area provide a benchmark for Corporations to study. *Piyawara*, the early child care and development (ECCD) project, is a huge undertaking executed with an integrated holistic community approach. The small administrative structure (just one passionate individual) and understated branding synergies show corporate accountability of a high ethical nature rare in the corporate world. Hemas is also supervising and managing the funds donated by New York based Sri Lankan Venture Capitalist/Entrepreneur Raj Rajaratnam to three leading Sri Lankan corporations for rehabilitation and reconstruction of tsunami damaged houses. In this context Hemas is overseeing and managing the building of 200 houses in Kalmunai.

Impact of government policy

While the closed economy of the 1970's was considered draconian and inward looking by free market commentators, it had the effect of driving entrepreneurs and companies to explore new business opportunities. Nationalization of plantations, import restriction, and a system of credits for exports and import substitution (FEECs[1]) created the impetus for entrepreneurial businesspeople to look outside their established markets in order to grow and to explore new opportunity areas for export. Hemas too was affected by these policy changes and while retaining its pharmaceutical business, ventured into businesses as diverse as hotels, apparel, gems & jewelry and labour recruitment for foreign employment. What these businesses had in common was the fact that they required little or no capital investment and were avenues to earn valuable foreign exchange. However, since these were not part of a cohesive business strategy, many of them eventually proved to be unsustainable. With the opening of the economy in the late 1970's, the Hemas group, including their stalled pharmaceutical business, once again flourished, this time under the direction of the next generation of family members.

Overall it is clear that Hemas has operated despite any particularly enabling policy environment. Sri Lanka's early opening of the economy vis a vis its regional competitors did not create a strong internationalizing of business ventures, despite the smallness of the local economy. We see that other than the export promotion incentives of the 70s that made the company go into tourism, gaining pioneering status for Clogard and some recent BOI tax holidays for investment (garments, power and generic drugs), Hemas has not received any other benefits through policy incentives, an enabling environment for project expansion or for technology transfer.

The path ahead

Hemas is in the process of managing the transition from a low profile private family business to a modern, publicly listed, investor friendly conglomerate. Some of the operational challenges facing the company are the following:

- ***Managing Culture Change***: Hemas must manage the impact of the changes in its business practices and employee relations, to maintain companywide morale.

[1] Foreign Exchange Earned Credit

- ***Attracting and Retaining Talent:*** While compensation packages appear to be competitive in the industry, Human Resource development and succession planning will be important emphasis areas over the next few years
- ***Focusing on Core Competencies:*** There appears to be a need for clear strategic guidelines in diversification planning and scenario setting, where focus on core competencies play a larger role in guiding new business decisions.
- ***Refining Corporate Roles and Responsibilities***: Hemas Holdings' executive directors perform as functional heads, making it difficult to step back and view areas that run across all business segments, such as human resources, long term management, and business strategy.

The company is looking for growth through leveraging its logistics, marketing and distribution capabilities and through acquisitions. While each sector has ambitious growth plans in competition with other sectors, Hemas remains a conservative company at heart. Its future plans will continue to be influenced by the personalities and culture of its present major-shareholder managers. The key challenge will be to continue to transform itself and sustain growth on its 5X vision[2].

While Hemas reaffirms its commitment to areas that provide synergies or economies of scale, it will be under market pressure to grow by acquisition to meet its top-line financial goals. One key concern is that it might be tempted into acquisitions or ventures in non-strategic areas for short-term gains. On the other hand, the company has shown an ability to correct mistakes and exit promptly from sectors with diminishing prospects. Another concern is that the company is still focused on Sri Lanka, with no real attempt being made to build export markets or go offshore to the Maldives or India. Eventually, Hemas will run up against the constraints of a relatively small domestic market in Sri Lanka. It will need to compete more globally to sustain its desired growth.

[2] Increasing the share price to 5 times its IPO value by 2010

1 Background

The hallmark of any successful business is its competitive performance in the markets it operates in and its capacity to deliver continuous bottom line growth. Theoretically, best practices, capacity to innovate, strategic intent and vision, ability to attract good people, facility to leverage core competencies and clearly defined competitive advantage are characteristics often said to make a difference. This study undertaken by The Competitiveness Program of Sri Lanka (TCP) and funded by the Agency for International Development (USAID) attempts to look at the evolution and characteristics of a successful Sri Lankan business, and understand the external context, such as policy, and the internal drivers that made this success possible.

Sri Lanka was the first market in South Asia to open its economy. In many dimensions, its performance has been paradoxical; high quality of life with low levels of productivity, high literacy and education with low levels of graduate employment, high political and ethno-civil instability with a democratic system of governance and relatively progressive macro-economic policies hampered by dysfunctional infrastructure implementation. A study of Sri Lanka's international competitiveness seven years ago concluded that while the country's overall economic performance was above the Asian average (Sri Lanka's score was 80 against the score of 73 for Asia - excluding Japan and NICs) its international competitiveness index was much lower than the average for the same Asian group of countries (Sri Lanka's score was 34 against Asia's 45) (Price-Waterhouse-Coopers, 1998).

Notwithstanding studies that try and establish national level scores there are examples in Sri Lankan of companies that have developed world-class capabilities, products, partners and practices. Other companies have evolved distinctly local identities, and successfully taken on global multinational giants in local markets , to create strong category contenders that have established brand and corporate equity in diverse market segments.

This study explores the evolution and success of one Sri Lankan business group that has developed some of these capabilities. Hemas Holdings Limited (Hemas) is a diversified business group that has sustained growth over the decades since independence. Growth is hard enough to achieve at the best of times but we have chosen a firm that has managed and sustained a record of growth over a historical span of time encompassing ethnic and civil conflict, closed and open economic policies and downturns in markets, changing socio and economic behavior and increasing technological change. More recently Hemas has managed the difficult transition from a small family-owned and run business to one that is still family-controlled, but now a widely diversified group of companies. It is a company, that has gone public, is professionally run and well set to manage and sustain its exceptional business performance. We will use an internationally prevalent template that is relevant to its business context to map out how the company drives its operations and where it is today in terms of globally established characteristics of excellence.

The Competitiveness Program (TCP) embarked on this study based on discussions with the Secretary of the Ministry of Industries and Investment Promotion (MOIIP) and the Director, Office of Economic Growth, USAID. TCP is a USAID-sponsored project designed to help key industries in Sri Lanka achieve international competitiveness and is being implemented by Nathan Inc. and J. E. Austin Associates. The program primarily provides technical assistance to private sector led industry-based initiatives to improve competitiveness. The program also partners with the Government of Sri Lanka and private sector groups to examine policy obstacles to improving competitiveness and to promote public awareness of competitiveness ideas as an engine for development in today's economy.

The MOIIP and USAID have expressed a desire to understand the following:

1. What were key business decisions over the course of a successful company's growth history and on what basis were they made?
2. What drove it to change business direction, diversify or implement aggressive

growth plans?

3. What factors enabled management to take the risk, if any, associated with those decisions? What competitive challenges were faced?
4. How does an open market economy like Sri Lanka, continue to maintain a reasonable rate of growth performance without demonstrating a critical mass of business competency in competition?

In addition, USAID is interested in the following:

1. How did successful companies find or develop their managerial, professional and technical staff?
2. How have working conditions evolved in response to a more competitive global market place?
3. What makes a company the best in its class? How do its business practices differ from those of the rest, be they related to strategy, product technology, marketing or human resource management, or production operation?
4. What are the learning outcomes from best practices of an organization to others? Is it the leadership, core value, a workforce of high-IQ people, or a instinct for leveraging uneven playing fields in policy and access to capital which sets an organization above the crowd

2 Case Study Goals and Methodology

2.1 Objectives

- To provide insight into factors underlying the ability of select Sri Lankan Companies to compete successfully.
- To identify factors that enabled corporate successes- internal and policy related
- To highlight successful behavior of local companies for others to emulate

2.2 Methodology

While descriptive as well as inferential statistical techniques have proven to be useful in the discovery process of general business behavior, the in-depth company case-study methodology has sometimes produced even deeper understanding and insights into best practices of sustained company performance and success.

The initial approach will be to document a case study and analyze successful Sri Lankan owned businesses that have managed to grow significantly since the opening of the economy. The company chosen was screened for performance criteria - sustained year on year growth in turnover profits after tax over the last decade; earnings per share, market capitalization, total assets and high local market standing as a business success. Qualitative hurdles, such as being fully Sri Lankan owned and managed, and a subjective assessment of the company's inherent potential to offer key learnings that would be of interest to other Sri Lankan businesses were also applied. It was important that the first firm selected was either a successful exporter or demonstrated ability to compete with global competitors in the local marketplace.

The methodology adopted was secondary historical research, financial analysis and interviews of key personnel as follows:

1. The study reviewed available published written material including, official and other publications, data on company's history and performance, organizational structure, business strategy etc. Independent and internet-based research reinforced the analysis.
2. Interviews were conducted with key players in the firm familiar with the history, as well as others who could shed light on the historical development such as CEO, HR Director/ manager, Marketing Director, Finance Director, Business Unit managers, and any other relevant person. (See Appendix A4)
3. A structured questionnaire was used as a point of reference with the preliminary CEO interview, but all interviews were casual and free flowing (See Appendix A5)
4. With regards to the area of workforce development, interviews were also conducted with a few select selected middle managers, and longstanding employees. Performance evaluation documentation was also reviewed

3 Cultural Context and Company History

3.1 Family Businesses

In a recent business leaders forum[3], Husein Esufally, the CEO of Hemas, presented a cogent argument that family-owned businesses “can compete with the best”. A study of Hemas certainly gives hope to other family businesses in Sri Lanka that adopting some of Hemas’ business ethic and discipline increases the chances of similar success. As Husein aptly defines it a family business is, in a narrow sense, one where several generations of the same family are directly involved in owning and running a business. In its broader sense it is several family members owning a controlling percentage of a company’s stock. Hemas falls within the purview of both definitions.

Global examples of family businesses range from Wal-Mart, a US$ 248 billion business, to Ford Motor Company and Samsung. Sri Lankan family-owned companies include Ceylon Biscuits, Carson Cumberbatch, Nawaloka Group, MAS Holdings, Associated Motorways, Ceylinco Group, Delmege Forsyth, and Abans. Typically, most family businesses do not last beyond a half-century or about three generations. In Sri Lanka the average “Third Generation” jinx is said to apply, as the usually frugal and disciplined founder (with a clear mission to succeed and plough back profits into the business) is replaced by less committed and often profligate second and third generations whose capacity to deliver on growth is further eroded by the fragmentation of power and control among multiple family owners. However, Hemas is now a 57-year-old business. How has it survived the pitfalls of other family businesses?

[3] LBR (Lanka Business Report)/LBO(Lanka Business Online) owned by Vanguard Group holds quarterly CEO forums

In attempting to answer this question, the entrepreneurial heritage and cultural traditions of the Borah community, to which the Esufally family belongs[4], cannot be ignored. Part of Hemas' discipline and ability to transcend the corrosive inward bickering on ownership, and feathering one's nest, which are typical of family businesses, can be attributed to the Borah culture and traditions. An example is Hemas' rational and sensible conflict resolution. Another worthy of mention is the community's strong emphasis on the value of hard work and recognition of its results. These are hallmark characteristics, strongly similar to the idealized "protestant work ethic" that many experts believe contributed to the success of commerce and industry in the western European economies and the United States. It is also similar to the Asia Pacific work ethic ascribed to by the Japanese, Korean and Chinese societies.

Some of the other reasons for Hemas survival as a family business are the third generation's willingness to work as a modern professional organization, open the business up to scrutiny as a public entity and drive this initiative with its ability to manage by consensus. Abbas Esufally, the eldest of the current generation in the business also highlighted another attitudinal characteristic that many of the elite families in business across all communities might agree on: "a belief in this country and a determination to stay and make money in Sri Lanka" despite the recurrent and diverse socio-political and economic uncertainties.

Most local family businesses are perceived to have the cavalier attitude of charging out all personal expenses and not ploughing back profits into the business: an attitude of "what I earn is mine". Such businesses are thus incapable of attracting and retaining external professionals who fear familial privilege over a culture of meritocracy and performance measurement. Hemas, however, established a transparent financial accounting system over 12 years ago, so that the businesses' people, assets and liabilities were clearly established, and performance and profit recognized and rewarded. It was also willing to look at the outside world to try to take in modern practices of business management and to think "big".

[4] For cultural and business heritage of the Borah community, see *Appendix A*

Husein Esufally's overriding contribution to the company has been to rise above such hurdles by focusing on getting the structure right. He has skillfully made use of outside consultants at key points of change initiation and driven the company towards the structure of a modern corporation - a holding company with autonomous business units.

3.2 The Hemas Culture

The Hemas culture is a blend of entrepreneurial spirit and a passion about business and making money. This includes being willing to look at new opportunities and areas, although in a conservative and highly financially disciplined way, being open to the input of professionals, being committed, and having high energy. The company itself is known for being ethical and honest, simplicity, innovation in building brands and representing good business partners and principles. An evaluation of its business history however reveals a myriad of other factors that has helped Hemas chart its way through changing times.

One is certainly its ability to transform itself over the years. The company has consistently been adept at managing change; from a pharmaceutical import company to a foreign exchange earner, from a single core business to a diversified company, from being a small family business to being professionally run, and most recently to becoming a listed, modern corporation. Hemas has been able to transform its attitudes, to think on a larger scale: to use expert consultants, bring in outside directors, and harness new technology.

Good managers know how to recognize and exit from bad decisions before they impact significantly on the business. Their 'win some, lose some, but minimize the losses' philosophy is a key strength in the Hemas approach to business diversification and new market entry. Hemas has demonstrated the ability to evaluate and take corrective action to reduce the outcome of unsuccessful business decisions - to take action before disaster strikes. For instance they moved out of tea and commodity trading in 1997 and more recently in June 2005 largely divested the apparel business. They acknowledged the failure of some products launched, and took lessons from them. They recognized the company's vulnerability to the mergers taking place between their overseas healthcare principals and set up a generic drug manufacturing facility to cushion the impact.

The makeup of the company has, from its early days in the form of separate businesses, been one that ran fairly independently under different family members. Although at times this organization was not conducive to concerted growth, it has certainly provided the company protection against downturns. Ownership was always explicitly laid out through a clear shareholding structure. At a time of directional turmoil the company was able to divide and divest some of these businesses among the various family owners and reorganize its corporate and ownership composition. This helped Hemas to focus on its future path and allow individual businesses the room to expand and change with the times. These divestments were achieved in a manner that was clear-cut and acceptable to all parties.

There are a number of special business traits and habits practiced by the Esufally family that were not learned at business school but can, in many cases, be traced back to the family's ethnic heritage. The Borah community embodies many customs and practices that are highly supportive of business success and continuity, including a practical and clearly laid out philosophy for conducting business. However, it is inherently chauvinistic towards women family members who, though often highly capable and educated in their own right[5], are not given a share of the business. The rationale behind this thinking is that it reduces potential for friction caused by in-laws entering the business and also avoids fragmentation of ownership. The family members all drive the same cars and share in company rewards equally, reducing family/business tensions. On at least two occasions family conflicts over the business have been resolved through the intervention of the Borah High Priest, circumventing legal tussles.

The Esufally family is regarded highly by their community as a result of their financial success and this also has implications on their relationship and access to their cleric. From early childhood they have been brought up listening to stories by their fathers and uncles about business and its nuances and given a feel for the

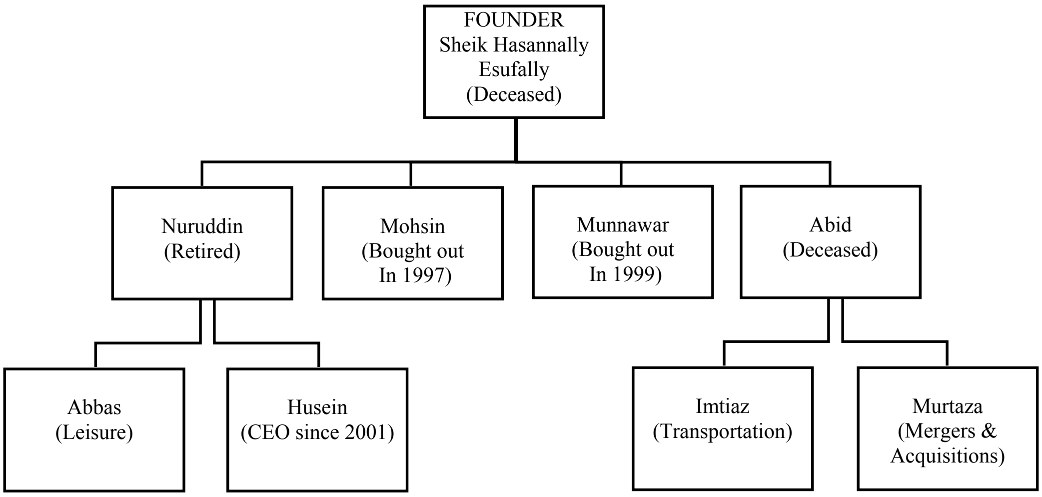
[5] A sister of Abbas and Husein Esufally is an entrepreneur with her successful clothing retailing business *Cotton Collection*

excitement and thrill of success. Proving themselves to the older generation through their own success in business has been a characteristic goal of the younger generation.

3.3 The Esufally Family

The Hasannally Esufally family of Hemas is a Borah family, descended from Mohamedbhoy Allibhoy who arrived in Ceylon around 1870 and established E.G. Adamally & Sons. The Esufally line descended through Mohamedbhoy Allibhoy's son Esufally and his son Hasannally Esufally, Hemas founder.[6]

Figure 1 - Family Structure



3.4 The Beginning

Hemas was born when Sheik Hasannally Esufally broke away from his brothers and E. G. Adamally & Company their family business and founded Hemas Drugs Limited. The company was incorporated in 1948 and started out as a chemist and druggist located on Dam Street in Pettah. It moved to its now landmark Bristol Street location, formerly the site of the Bristol Hotel, in 1951. Known as Hemas Drugs Building, it was constructed by Hemas' founder with the finest building materials of its time. The business was involved in three main activities namely: drug import and distribution, textiles and laboratory equipment. The family's real estate holdings included two tea estates producing high quality tea and the Hemas Drugs Building, which was largely a rental property.

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[6] S. Muthiah, *The Indo-Lankans* (Chennai: Nagaraj and Company, 2003), 131-142

Hemas took pride in its ability to build and maintain strong cordial relationships with its principals and suppliers and established a reputation for reliability and honesty. Its owners were very social and urbane individuals, who carried on business very much on the basis of personal relationships. Evidence of such relationships was seen in 1962, when Diparco SA of France (later bought over by L'Oreal) gave Hemas the license to manufacture two colognes it had previously distributed through its pharmaceutical business - .i.e Bien Être and Baby Cheramy. Diparco provided Hemas with product testing assistance at its own laboratories and on-site experts to help with setting up the local manufacturing operations and quality control. Hemas later took over the Baby Cheramy brand name, which Diparco was discontinuing worldwide.

3.5 The Early Years

By the 1960s while Sheik Hasannally Esufally remained active in the company as chairman, the second generation of four Esufally brothers had taken over the management of Hemas. The brothers divided the management of the business between them: Tea Estates (Nuruddin Esufally), Pharmaceuticals (Mohsin Esufally), Laboratory Equipment and Tenders (Munnawar Esufally), Legal and Administration (Abid Esufally). The company was by now recognized as being reliable and able to source products backed by reputable principals. The family used their network of relatives and contacts overseas to acquire agencies and products from foreign principals and suppliers. They also had access to expertise on their products, through suppliers and other contacts. Suppliers dealt with Hemas because they were assured of predictability and honesty in their dealings.

Employee Relations

Hemas has historically treated its employees as an extended family. The brothers had the talent of identifying good people and motivating them to do their best for the company and its growth. Once their trust was won, they backed their employees completely and many felt their lives were enriched by the experience of knowing and working with the brothers. Most employees considered the brother they worked under to be their mentor. Hemas' staff was not necessarily rewarded with large salaries, but together with its annual trip, end of year hamper, bi annual bonus and close touch with its owners, employees felt they belonged to a close-knit family. A high number of long-term employees felt strongly that Hemas would look after them for life.

For a further insight into Hemas' employee relations see Appendix A2

The early 1970's marked dramatic changes for Hemas as it saw its revenue severely reduced due to government policy changes. A predominantly import-driven company, Hemas' core pharmaceutical business was profoundly impacted by import and foreign exchange restrictions imposed after the United Front won a resounding victory at the 1970 elections[7]. Policy changes such as Foreign Exchange Controls, Land Reform, the Rent Control Act, and nationalization of private companies all had an overwhelming negative effect on Hemas' lines of business.

The State Pharmaceutical Corporation took over much of the drug sales that Hemas had previously enjoyed. Income from tea production was curtailed as the estates Stafford (350 acres in Nuwara Eliya) and Noorie (1000 acres in Deraniyagala) were subject to nationalization and land reform. Rent control reduced rental income from the Hemas Drugs building, where all except the basement and mezzanine floors were leased out. The family members were also personally subject to a recently introduced "wealth tax" on assets. All of these resulted in a significant financial strain on their individual incomes during this period. In addition to the foreign exchange needs to operate the company's import businesses, they needed access to foreign exchange for the education of their children overseas.

> ***1970's Policy Impact***
> *While the closed economy of the 1970's was considered draconian and inward looking by free market commentators, it had the effect of spurring entrepreneurs and companies to explore new business opportunities. Businesses were forced to look outside their established markets in order to grow and new opportunity areas for export and indigenous growth were more closely examined.*

The family was forced to look ahead and diversify its business interests, which included export oriented industries that were being promoted by the GSL at that time. Hemas ventured cautiously into many of these areas. Its motivation was the threat to the core pharmaceutical business and the need to earn foreign exchange under the FEECs[8] program to help existing import sectors. There was nevertheless a conviction that they could and would do what was required to be profitable in the new era.

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[7] In 1970, the United Front, a socialist coalition led by the Sri Lanka Freedom Party together with the Lanka Samasamaja Party and the Communist Party, won a two third majority in Parliament. Mrs. Sirimavo Bandaranaike became the Prime Minister.

[8] FEEC: Foreign Exchange Earned Credits – a program that allowed businesses to earn foreign exchange credit against their export earnings - introduced by the Sri Lanka government in the 1970s in an attempt to increase foreign exchange reserves.

While retaining its pharmaceutical business, Hemas looked at new areas and committed its energies into making these a success. Hemas dabbled in the hotel industry - taking over the management of two Maldivian hotels, the apparel industry – Cupid Industries Ltd. (with a partner), the gem and jewelry industry, labour recruitment for foreign employment, and commodity exports. While seemingly very diverse, what these businesses had in common was the fact that they required little or no capital investment and were avenues to earn valuable foreign exchange. Whatever capital was required for these ventures was sourced internally. However, by the early 1980s the company had exited many of these businesses as not sustainable due to financial non viability or the lack of management personnel.

Hemas in the 1970s and early 1980s bears the stamp of Mohsin Esufally's adventurous personality. An extrovert and unconventional thinker, he provided the innovation that Hemas needed at the time to grow, expand and become broad-based enough to survive. He won and began the cologne manufacturing operation and ran the pharmaceutical business, which was the main income generator for the company, and launched Hemtours in 1976. Mohsin began many of the businesses grown by the next generation of Esufally sons.

3.6 The Open Economy Years

The late 1970's heralded the open economy in Sri Lanka, when foreign exchange restraints were removed and imports flooded the market. Heavy government spending on accelerated hydroelectric and other large-scale infrastructure projects helped stimulate the economy. Sentiment in the commercial sector was strong as the real estate sector boomed and overall most mid to large size businesses grew and made profits. Due to the removal of import restrictions, Hemas' previously stalled pharmaceutical import business too flourished once again.

Coinciding with the opening of the economy, the late 1970s and early 1980s saw the entry into the business of the new generation of Esufally men, who had all graduated from universities in the United Kingdom. The following decades benefited from the renewed energy and dynamism the new generation brought to the business. The success of Hemas today can be traced to the business areas entered into by this younger generation.

Abbas Esufally, Sheik Hasannally Esufally's oldest grandson and the elder son of Nuruddin Esufally, was the first new entrant into the ranks of management in 1977.He was the only grandson that Sheik Hasannally saw in the business prior to his death in 1980. Abbas, a qualified Chartered Accountant in the UK, returned to Sri Lanka after having worked briefly in London and was given the helm of the recently launched leisure business of "Hemtours", which concentrated on the inbound travel industry.

In 1983 Mohsin Esufally, who had functioned as General Manager, retired from the company. He gave up his executive functions although he continued to have a seat on the board. This was a fundamental change for Hemas and one that would influence its future growth path. Mohsin had very much embodied the entrepreneurial spirit of Hemas. After his departure, Hemas concentrated much more closely on unlocking the potential of existing businesses rather than constantly exploring new ones. His exodus however created a vacuum that gave the returning generation of Esufally cousins the opportunity to fill.

Husein Esufally, Nuruddin Esufally's younger son, entered the business in 1981 after completing a degree in Electronics in the UK. The family policy at this time was to teach its younger members "on the go" by giving them each a business to run. Husein started off with an unsuccessful sugar trading venture, and then a cheese import venture, until finding success in the fledgling eau-de-cologne business, which he grew steadily into what is now Hemas' highly successful personal care business.

Imtiaz Esufally, the son of Abid Esufally, entered the business in 1984 having graduated with a degree in Accounting and Economics in the UK. He joined his father who was now overseeing the core Pharmaceutical business. He subsequently took over the outbound travel business of Hemdrug Travels, which had received IATA[9] status in 1982.

[9] International Air Transportation Association

Murtaza Esufally, Abid Esufally's youngest son entered the business in1992 after following in the footsteps of his father and obtaining a law degree in the UK. On his return, he began Hemas second venture into the apparel business – Hemas Garments.

Overall, the 1980s saw Hemas as a whole grow strongly, both in terms of turnover and profit. Most of its businesses were expanding and these profits were channeled into the trading business due to its high profitability and the company's desire not to borrow externally. The following section expands in more detail on the different business units, including their growth through the 1990's.

3.7 The Business Activities

3.7.1 Leisure

Around the time Abbas joined the company (1977), tourism as an industry had just begun to develop in Sri Lanka, with many of today's large players such as Aitken Spence and Jetwing entering the industry. However, despite the fact that the core pharmaceutical import business was doing well in the new open economy, there remained a reluctant to making capital outlays and incurring debt, even for the sake of growth. Hemas made no attempt to take an ownership stake in the hotel sector despite the complementarities with its leisure sector. Further, it allowed its management contract of two prime Maldivian resorts (now run by the Universal Group and Banyan Tree Resorts respectively) to slip away due to lack of in-house expertise.

> ***The Maldives:***
> *Of all participants in the leisure industry, Hemas was one of the first to identify and enter the now much sought after and now profitable resort market in the Maldives. While Hemas gave up its Maldivian interests in 1983 following the communal riots in Sri Lanka other local hoteliers, such as Aitken Spence Hotels, that followed now realize significant group profit contribution from the operation of Maldivian island resorts.*

Hemtours remained focused on the operation of tours within Sri Lanka alone, and as a result was badly affected by the temporary collapse of Sri Lankan tourism following the 1983 riots. Most of the late 1980s and early 1990s were spent recovering from the impact of these riots and also from the JVP terror campaigns of the late 1980s.

Figure 2 - Key Brands (Leisure)

In the late 1990s Hemas finally bought into the hotel sector, although indirectly, through ownership stakes in Serendib Hotels and Associate Hotels (both listed companies) and in Peace Haven resorts. Serendib Hotels owns three hotel properties, (Sigiriya, Serendib and Dolphin), Associate Hotels owns one (Lihiniya Surf) and Peace Haven is a property for development located in Tangalle.

3.7.2 Transportation

This business segment was focused on outbound travel, specifically for corporate clients. Hemdrugs Travels (later to become Hemas Travels) had been set up in the 1970s and soon specialized in outbounds leaving the inbound area to Hemtours. The company received IATA accreditation in 1982. The business grew at a steady pace throughout the 1980s. As a result of its close relationships with airlines it began freight forwarding operations in 1992, covering both air and sea cargo. It has recently set up a clearing office in Chennai, India, to expand its interests in this area and hopes that this will be the start of a network in the local region. In 1994 and 1996 the transportation sector added General Sales Agencies (GSAs) for Malaysia Airlines and Emirates Airlines respectively and between 2000 and 2004 it added GSAs for a further six airlines including British Midland, Druk Air and LTU.

3.7.3 Pharmaceuticals

During the 1970's, sales had been largely wiped out by the establishment of the State Pharmaceutical Corporation (SPC). During this period, all hospital drug supplies had to be procured through a tender process via SPC – there was no "private sector" market. Income was only through commissions on sales. Despite near zero pharmaceutical sales, Hemas held on to its sales team during these difficult years selling non prescription items and other consumer product. This policy paid off following the opening up of the economy in 1978, when Hemas quickly restarted this business and began to formalize its pharmaceutical marketing and sales effort.

Historically, Hemas' sales and marketing efforts were based on direct door-to-door approach and primarily through associations with the medical profession. In the early 1980s the business still had annual sales of around Rs.5 million only (although profit margins on products were still very high). Including sales of other non-pharmaceutical consumer products such as thermos flasks and prunes, the combined annual sales of the division were around Rs. 9.6 million. With the growth in the liberalized economy and a renewed focus by the company sales grew at a tremendous pace. The growth spurt began in 1984 with annual pharmaceutical sales more than doubling from Rs. 5 million to Rs. 12 million. Over the next six years sales had grown twelve fold to reach Rs. 144 million.

Hemas became known as one of the fastest growing pharmaceutical companies in the country. Its agencies included Leo Pharma, Ayerst, Schering, and Seven Seas. The Seven Seas agency notably had been with the company for many years and, being a supplement, had been sold throughout the 1970's years. Ranbaxy, its highest selling agency, came to Hemas in 1985, as the company aggressively and successfully added additional brands to its range.

Figure 3 - Key Brands (Pharmaceutical)

In 1989 Hemas became the largest pharmaceutical supplier of imported drugs to the private sector healthcare industry, a position it maintains today with a 16% market share. During the 1990s Hemas also became the leading supplier to the state healthcare sector. The 1990s witnessed mergers among large international drug companies, many of who were represented by Hemas. Recognizing the company's potential vulnerability to changes in their overseas healthcare principals, and the resulting risk of losing the agencies, the company set up a generic drug manufacturing facility in Sri Lanka, which now accounts for 10% of its pharmaceutical sales.

3.7.4 Personal Care

From its inception in 1962, the eau-de-cologne manufacturing business had been operating from Sheik Hasannally Esufally's sprawling residence on Flower Road. The property comprised the house, a banana plantation, poultry runs and the Bien Être and Baby Cheramy cologne factory. By the early 1980s, around 5000 units of 50ml and 100ml bottles were being produced per month, with just eight people involved in manufacturing, and a separate sales force of 20-30 handling sales. The business took its first step towards becoming the future "Personal Care" division of Hemas, when the cologne factory was moved to Elakanda in 1985. By this time Husein Esufally was in charge of the cologne business, and was committed to making it grow.

Cheramy was Hema's first big volley at competitor Unilever, whose Pears Baby was well entrenched in the market. Baby care products was a very difficult category to penetrate in the Sri Lankan market as customers were keyed to established brands which they trusted and perceived as high quality. Interestingly, group capabilities in the Pharmaceutical division helped build retail strengths in a distribution channel (retail pharmacies) that Unilever had less access to. Cheramy used the combination of consistent quality with strong and consistent integrated communication strategies and a key perfume differentiator, which showed Hemas' ability to build strong brands on par with the best of multinationals. Hemas' baby clubs and vaccination programs, and a tie-up with UNICEF all added to the flair and depth of brand presence.

Soon the Baby Cheramy range was extended to include cream, talc, soap (manufacturing outsourced to Upali Industries) and later baby oil and shampoo. Around 1988 the section set itself a goal of developing a new toothpaste and shampoo

– two consumer products with the highest market penetration. Its first innovation, Marvel shampoo, came out in 1990 but was not a success. But Husein Esufally and his team were by now committed to new product development. An Indian innovation (*Promise Toothpaste* by Balsara Hygiene Products) at that time guided them in the direction of a toothpaste with a local herbal ingredient - clove oil. In 1992 Clogard toothpaste with its distinctive clove flavour was launched. Clogard was a significant milestone for the Personal Care division and one that spurred it on to beat the Pharmaceutical business and become the flagship business in the Group.

In the past, competition between each division had spurred the other on to achieve higher sales targets, but pharmaceutical sales could no longer keep up with the turnover of the Personal Care division. Growth in personal care product sales in the early 1990s was tremendous. Sales more than tripled between 1989 and 1992 from Rs. 60 to Rs. 200 million and went on to reach Rs. 340 million over the next two years.

These results were achieved through the launching of new branded products (Clogard, Dandex, Kumarika etc) and later the acquisitions of branded products (Goya, Gold, Supersoft) and distribution of branded products (Procter & Gamble). The sales atmosphere was highly convivial and charged with energy[10]. The sales force would set highly ambitious targets, often double that of the previous year and then did whatever it took to achieve them. The division held annual sales conferences to celebrate successes and upon exceeding sales of Rs. 500 million in 1995 took its entire sales force on a trip to Malaysia.

Clogard Toothpaste:
Clogard was a tremendous success for Hemas. Not only was it a local brand and a product appealing to local taste, but it was also the local underdog fighting against the huge multinational. Clogard brought the Hemas name to the lips and minds of the general public. Expertise for its manufacture came from unconventional sources - Hemas' suppliers and a USAID consultant. Its machinery was bought second hand from Lankem. Its storage vessels were designed by Hemas' staff and manufactured locally. Shortly after Clogard was out on the shelves, Unilever who had enjoyed over 95% share of the toothpaste market launched a court case to keep Hemas out of the toothpaste market. Unilever lost and Hemas fought back, ploughing100% of the years advertising budget into Clogard. Its advertising campaign openly adverted to the legal battle, and Clogard reached a 30% market share.

[10] The sales division even composed a Hemas song.

Personal Care continued its wave of new product launches into the mid 1990s, and Hemas became a well-known name in the Sri Lankan personal care industry, second only to Unilever. Its flagship brand remains Baby Cheramy, with Clogard contributing significant revenues.

Figure 4 - Product Launches 1962-2005

1962	Baby Cheramy & Bien Etre Colognes (manufacture)
1985-89	Lakme, Godrej, Seven Seas (agencies); Extension of Baby Cheramy range to talc and cream; Capri Cologne
1991	Baby Cheramy Oil and Shampoo; Marvel Shampoo (failed); Dandex Shampoo
1992	Clogard Toothpaste
1993	Baby Cheramy Relaunch
1994	Pro Sport Cologne; Images (failed)
1996	Kumarika Shampoo; Activ Toothpast, Piknik (Foods) (both failed)
1998	Procter & Gamble brands; Goya, Gold Supersoft (all from Reckitt)
2001	Debutante (failed) (from Unilever); Kumarika Hair Oil
2002	FairRose Fairness Cream; Clair Skin Care; Diva Detergent
2004	Germguard Toothpaste; Fems Napkins, Nimex Tissues (both acquired)
2005	Pro Sport razors; Rockers Potato Chips; Velvet Soap

The division is now targeting the relatively untapped male consumer with its hair oils and colognes. As part of its efforts to expand its personal care products range, Hemas recently acquired businesses producing sanitary napkins and other paper products, and set up a soap manufacturing facility to manufacture Baby Cheramy soap (previously outsourced) and its own brand of toilet soap – Velvet – to compete directly against Unilever's Lux brand.

Figure 5 - Key Brands (Personal Care)

Hemas Personal Care business division today accounts for 45% of the Hemas Group Profit (33% of Group Turnover) and new products developed over the last 3 years account for 20% of the business. This business' success can be attributed to its strategy of building brands relevant to the Sri Lankan consumer, using local ingredients. Its main competitors are the two multi-nationals, Unilever and Proctor and Gamble, as well as other local players.

3.7.5 Strategic Investments

Hemas Garments, the apparel business, began operations with a 100-machine facility and grew to 450 machines by the early 2000s. This venture was started to take advantage of the generous government incentives being offered to the apparel industry and in search of the tremendous success that some early participants had enjoyed. However, Hemas was too late an entrant to the area to share in that success. Its exports were almost all on a non-quota basis and the company struggled with operational efficiency issues that its competitors had worked out in the early years of the industry.

Hemas Development began in 1997 as a Board of Investment (BOI) approved rental property development and infrastructure projects business. So far its only project has been Hemas House – an eleven-storied modern office complex located at Braybrooke Place, Colombo 2 and was completed in 1997. Except for Hemtours and Hemas Travels, most of 70,000 square feet is rented to outsiders.

3.8 Significant Company Reforms

This section covers the three most significant milestones in the transformation of Hemas from a family owned business to a large corporation. These are the formalization of the corporate structure in 1993, the restructuring of the ownership in 1999 and the IPO in 2003.

3.8.1 Corporate Restructure – 1993

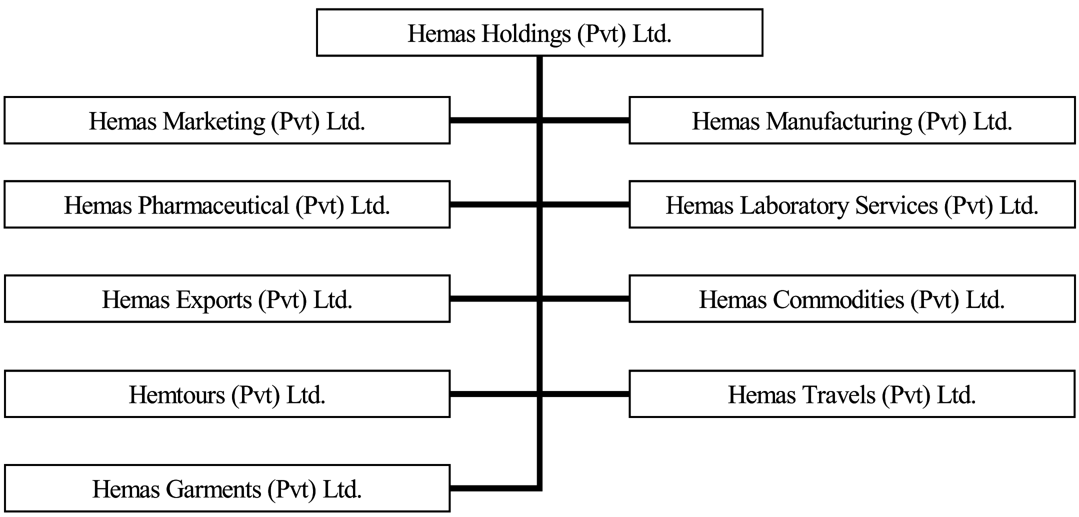
The early 1990's were a time of tremendous change for Hemas as it attempted to manage the metamorphosis of the company resulting from the high growth of the previous decade and its varying impact on different units. In 1993 the company undertook a fundamental corporate reorganization, through which it attempted to define itself along the lines of a modern US corporation.

Prior to 1993, the company had a single combined balance sheet for its nine companies, making performance measurement of separate business activities difficult if not impossible. As a result, planning and strategy were also handicapped. During its history, the subsidiaries and associate companies had been added to its structure on an ad hoc basis. (See Appendix A6 for structure).

Hemas brought in the outside expertise of a management consultant with funding assistance from USAID. and an accountancy firm to separate the assets, liabilities and people of its diverse operations. It also took this opportunity to appoint some of its senior managers to the board of these companies. Subsidiaries were organized by sector under the umbrella of the parent company and the name of the parent company was changed from Hemas (Drugs) Ltd. to a more general Hemas Holdings Ltd. to reflect this change of structure. The new structure of 1993 is shown below.

Transitioning from a family-run to a corporate business structure
The issues Hemas was grappling with at this time are those familiar to any family business: a lack of forum for discussion and criticism of the business, a blurring of the division between business and family affairs, a difficulty attracting and retaining professionals, a lack of accounting transparency. What differs is that Hemas had the strength to attempt to address these issues directly rather than piecemeal, by bringing in professionals to advise on and structure this transformation

Figure 6 - New Corporate Structure - 1993



3.8.2 Ownership Restructure – 1999

Hemas went through significant ownership reorganization in the late 1990s. As the number of family members involved in the business grew, divergent views arose as to the running and future direction of the business. The struggle was primarily a clash between the business values and views of the older and younger generations. Hemas had been in business for half a century by this time. The business methods and areas of growth were now significantly different from what they had been in the 1950s and 1960s. While key values such as prudence, conservatism and simplicity had been trademark features of the business, these values were no longer sufficient for dealing with the complexity of the business environment in which it was now operating.

The focus of the company was temporarily diverted away from its business activities to center on resolving these conflicts. As it became clear that certain fundemental differences could not be resolved, some of the family took a decision to move out. One of the major challenges was establishing a value for shareholders who wished to exit the business. This was accomplished through mediation by the high priest based on independent valuation by a professional accounting firm. It was agreed that those family members who chose to depart the business would take certain businesses that were managed by them[11] and be paid cash to cover the difference in value between these businesses and their overall shareholdings.

The remaining businesses, which make up the current Hemas Holdings, were now owned by four 3rd generation Esufally men - the current day majority shareholders. This was a significant shift from the previous shareholding of 13 family members spanning two generations. The four new owners of Hemas Holdings however faced a dilemma in financing the buyout since most of their own wealth was already locked in Hemas' cash rich businesses and the company itself could not buy the shares[12]. As a result, an innovative structure was used to finance the buy out. Counting on Hemas' future earnings to generate sufficient cash to make the payments, the four new owners used their shares in the company as collateral to pay for a bank guarantee which assured the exiting family members of regular annual payments over the next 3 years.

[11] Hemas Exports, Hemas Laboratory Services, and Hemas Commodities

[12] The Company's Act No. 17 of 1982 specifies that a company cannot finance the purchase of its own shares.

Hemas Holdings then consolidated its remaining activites under five sectors: Healthcare (made up of Hemas oldest business of pharmaceutical sales, and generic drug manufacturing), Personal Care, Transporation, Leisure and Strategic Investments. The company also exited from the marketing of branded food at this juncture.

3.8.3 The IPO – 2003

The next and most significant milestone in Hemas' evolution took place when the company was listed on the Colombo Stock Exchange (CSE) in October 2003 following a much anticipated, Initial Public Offering (IPO) that was 11 times oversubscribed.

	Number of Shares	*Price*	*Proceeds*
Issue of New Shares	*8 mn*	*Rs. 50*	*Rs. 400 mn*
Offer for Sale of existing shares	*4 mn*	*Rs. 50*	*Rs. 200 mn*

The share price shot to an intraday high of Rs. 100 on its first day of trading, double its issue price[13] of Rs. 50 before closing around Rs. 80. Unable to handle the extraordinary volume of orders generated as a result of the IPO, the CSE's trading system crashed briefly during the day. Hemas well exceeded analyst projections for its future growth, and year on year has provided upside earnings surprises. Investors who purchased and held Hemas shares from the time of the IPO have enjoyed a total return of 225% as of the end of September 2005.

Why an IPO?

Why does a privately owner family business go public? In the case of Hemas, it primarily had to do with unlocking value for its shareholders.

The IPO was a method for the owners to access some of Hemas significant wealth by providing a liquid market for their share holding. At the time of issue itself, while issuing 8mn new shares the owners sold 4mn of their existing holdings realizing Rs. 200 million in cash. The overall outcomes of the IPO were:

1) *cash realized by its owners*
2) *greater public awareness for the company and its business activities*
3) *additional funds to finance its thermal power investment, and*
4) *a new means of funding established for the company*

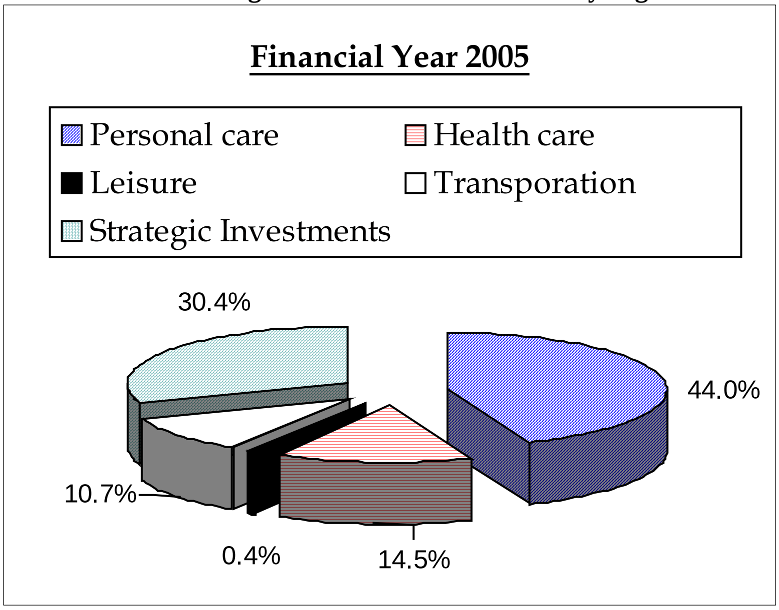
[13] The Issue price was made up of a Rs. 10 book value and a Rs. 40 premium.

3.9 Hemas Today

Hemas areas of business activity in the present day are centered on personal care, healthcare, transportation, leisure, power, and property management. The bulk of Hemas' profits still accrue from the Personal Care business. Despite a fall in turnover in the last financial year (2004/5) of Rs. 44 million or 1.6%, (due in part to the termination of the Rs. 550 million turnover Proctor & Gamble distribution agreement - worth approximately Rs.25 million in profit), Personal Care still contributed 44% to group profit.

3.9.1 Business Unit Contribution

Figure 7 - Profit Contribution by Segment



Profit from Personal Care grew by 18 % in the financial year 2004/5 and results for June 31, 2005 show this trend continuing with Personal Care Q1 profits up 30% versus the previous year. Healthcare contributes a steady 14% to the Group's profit. The segment called Strategic Investments, which comprises power, apparel (now 70% divested) and real estate was responsible for approximately 30% of turnover and profit in the financial year 2004/5. The full effect of the divestiture on this sector's contribution to the group remains to be seen, but the apparel sector is understood to have contributed approximately Rs. 40 million or 5% to group profit in 2004/5.[14]

The remaining sectors, Leisure and Transportation, tend to be much more susceptible to shifts in the economic and political environment. Leisure, the most volatile, contributed 16% to profit in the financial year 2003/4, but only managed to contribute

[14] Proceeds from the sale of the apparel business were booked as profit during this period.

0.4% in 2004/5 because of low occupancy following the December 26, 2004 Tsunami. Transportation grew well from a 9% contribution in the previous financial year to 11% in 2004/5. This growth trend continued strongly into Q1 2005/6 with the sector posting a profit growth of 50% over the previous year's corresponding quarter.

3.9.2 Group Performance

Hemas' growth has been consistently strong over the past six years. In 2005 the company achieved 36% top line and 31% bottom line growth, compared with 23% and 53% respectively for 2004, due to low margins in the Power sector.

Figure 8 - Group Revenue

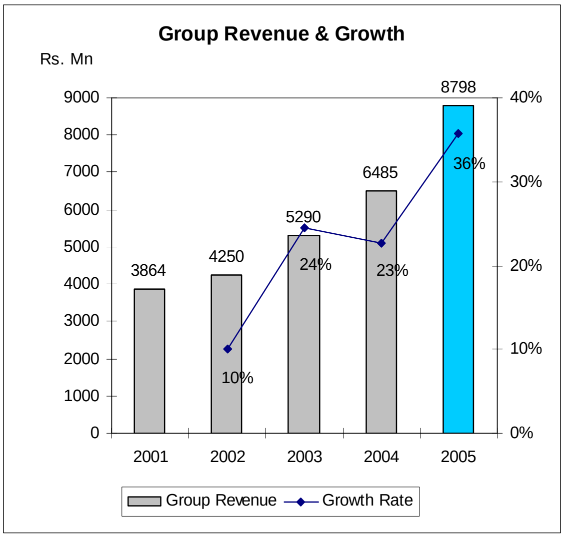


Figure 9 - Profit after Tax

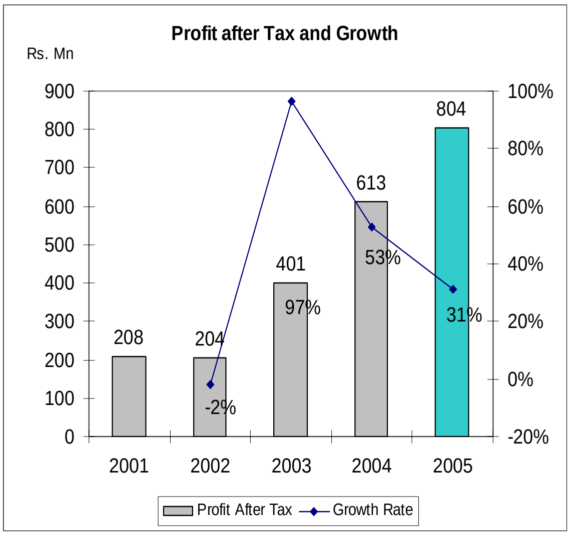
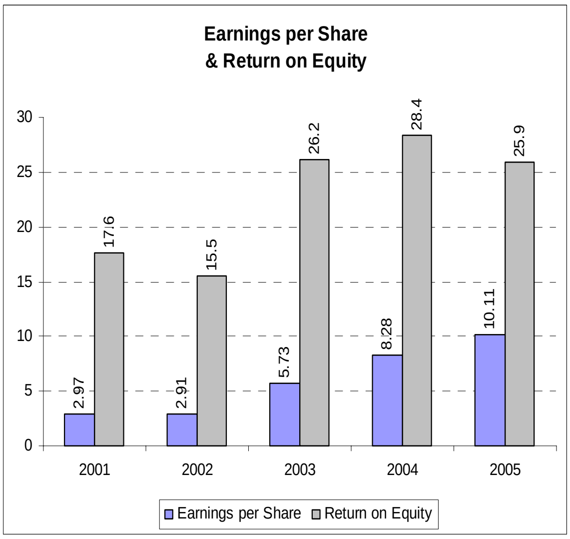


Figure 10 - EPS & ROI



The company's latest earnings per share figure is a healthy Rs. 10.11 and has grown from Rs. 5.73 in 2003. Its P/E ratio (Price per share /Earnings per share) is 10.8 versus a market P/E of 17.7 for the diversified sector15. The company's share price upside is somewhat constrained due to a lack of liquidity in trading as the majority of its shares is still held by the family.

[15] The CSE diversified sector into which Hemas falls is made up of such blue chips as John Keells Holding and Aitken Spence

The family further reduced its holding from 82% to 75% in October 2005 through a divestiture to three local and four foreign institutional investors. Eight million shares were sold at a price of Rs. 130 each.

Since 2003, Return on Equity and Return on Capital Employed are both well into the 20% range, dropping only in 2005 as a result of Hemas' Rs. 600 million capital investment in Heladhanavi, its thermal power joint venture. Even prior to 2001 Hemas' Return on Equity and Return on Capital Employed were typically very high.

Figure 11 - Capital Employed

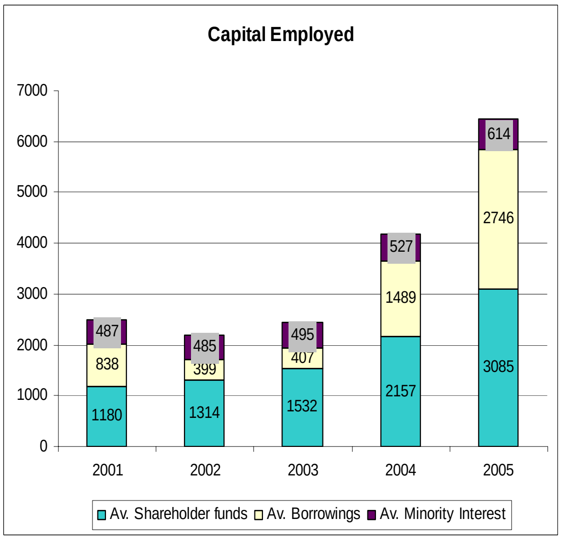
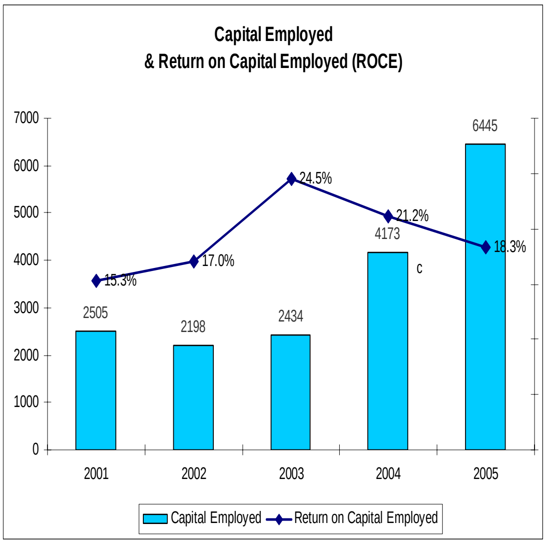


Figure 12 - Capital Employed and ROI



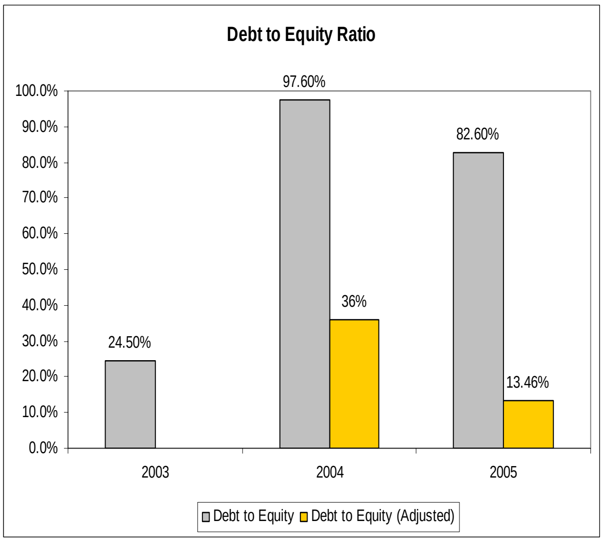
The reason for this is the company's past record of not entering into industries and areas that require major capital outlays or a long development period. Instead it focused on service sectors such as tour operations, airline GSA's and freight-forwarding which have shown strong returns on capital investment in the near term. Another contributing factor, however, that must be considered is the fact that Hemas brand building exercises are expensed rather than being reflected in Capital Employed[16].

Due to its conservatism and family heritage the company has been reluctant to borrow externally from the domestic market except for short-term purposes. The composition of Capital Employed as shown above indicates its high use of shareholders funds. Historically, most of its profits appear to have been reinvested in the business. The

[16] Capital Employed is made up of Shareholder Funds, Borrowings and Minority Interest

company has grown and prospered as a result of such reinvestment. From a portfolio management perspective the decision to reinvest has been well justified. For the four years prior to its public listing, (and following the 1999 ownership restructuring) the company maintained an average annual dividend payout of 23%, even in the face of bonus issues that increased shares issued from 3 million to 70 million during these years.[17]

Figure 13 - Debt to Equity



The company's long-term debt has historically been extremely low. Prior to Heladhanavi total borrowings for the group were a mere Rs. 412 million – providing a Debt to Equity ratio of 25%. Presently, total borrowings of the group (excluding Heladhanavi) are just Rs. 477 million. With Heladhanavi total borrowings come to Rs. 2.9 Billion and a Debt to Equity ratio of 82.6%. This Rs. 6 billion thermal power project is highly geared as is typical for high investment infrastructure projects of this nature and was 80% financed by bank borrowings with Hemas and its joint venture partner Lakdhanavi contributing Rs. 600 million each.

Total assets have risen sharply in the past two years again as a result of Heladhanavi as well as acquisitions in the personal care and hotel sectors and investment in an Enterprise Resource Planning technology and a soap manufacturing facility. Hemas Cash from Operations (COP) has grown five fold in the past five years.[18] This reflects the fact that the company is in businesses with strong margins and high turnover. COP in 2002 was. This cash provides Hemas with plenty of cushion for debt service on any new borrowings, the ability to pay dividends as well as a war chest for future acquisitions.

[17] Data on historical dividend payouts has not been provided.
[18] In particular, cash from operations increased sharply in 2005 due to the increase in depreciation expense from setting up the power plant together with a significant drop in receivables outstanding.

Figure 14 - Total Assets

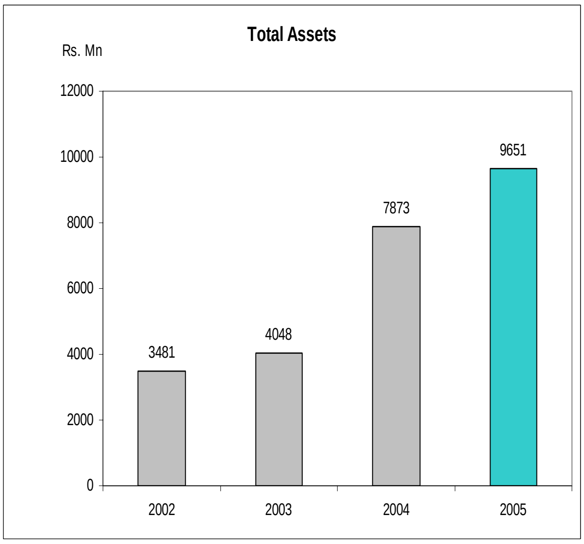
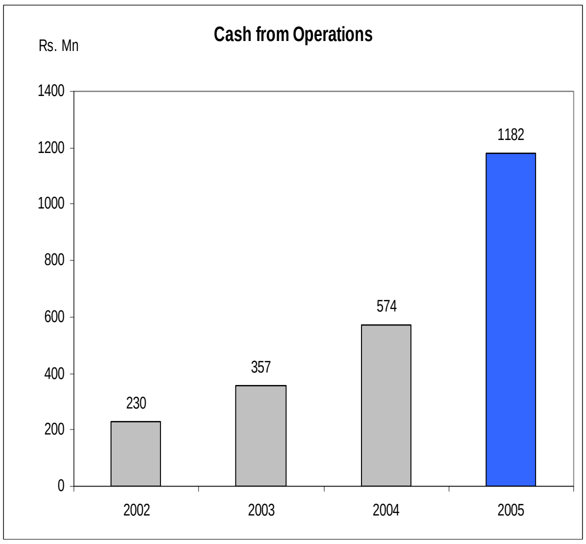
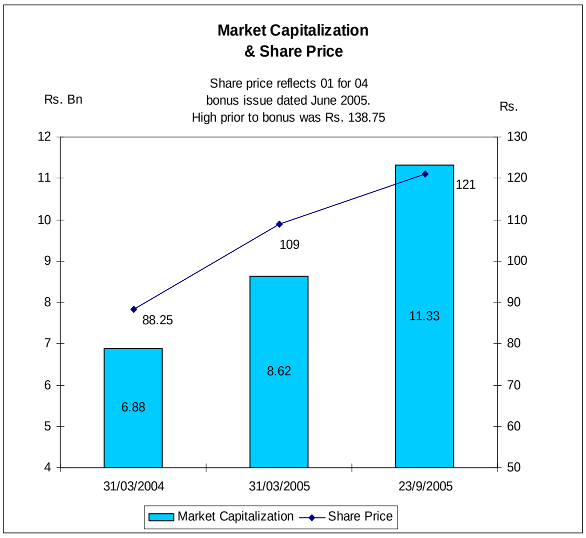


Figure 15 - Cash from Operations



Today the company's market capitalization has climbed over Rs. 11 billion. Its share price has reached Rs. 121 following a recent 1 for 4 bonus, when its price adjusted from 138 to 103. This issue was done primarily to enhance liquidity in the market.

Figure 16 - Market Cap & Share Price



Due to the diversified nature of its present business segments, the group is protected from major changes in turnover resulting from an economic downturn. Stock analysts prize the company for its exposure to less volatile sectors of the economy, steady earnings potential, high return on capital employed and management commitment to providing shareholder returns. In its mission statement, Hemas has promised its shareholders the delivery of the best ever returns a listed company has given in the first 7 years of being listed.

3.10 Path Forward

Hemas today is looking for growth through acquisition and the leveraging of its logistics, marketing and distribution skills. While each sector has ambitious plans for growth in competition with other sectors, Hemas remains a conservative company at heart. Its future plans will continue to be influenced by the personalities and culture of its present major-shareholder managers. The following table outlines Hemas future direction as presented in the company's 2004/2005 Annual report.

Table 1 – Future Direction

Strategic Business Unit	Current Status	Future…
Healthcare	Imports and distributes high end drugs, manufactures generic drugs	Leverage long standing relationships within the industry to expand into other areas of Healthcare.
Personal Care	Develops, manufactures and distributes personal care products. Recent entry into detergent and food markets.	Continue focus on core brands along with emphasis on new product development and acquisitions to enter allied segments.
Transportation	Operates outbound travel agency, freight forwarding business and 8 GSAs for airlines.	Expand offerings of Logistics services – Joint venture with Hellmans Worldwide.
Leisure	Provides tour packages to tour operators, owns direct and indirect stakes in a few hotels and hotel development properties	Explore opportunities in the high end resort market
Strategic Investments	• Owns 50% of a 100 MW thermal power plant. • Owns and operates Hemas House - a modern office complex.	Explore further opportunities in the power sector.

While some may trumpet its venture into the power sector as a bold move, Hemas investment in Heladhanavi may well be viewed as an investment in a sophisticated, "return enhanced" ten-year sovereign bond. By combining a ten-year power purchase agreement with the government and an interest rate swap agreement, Hemas has effectively locked into a fixed rate US$ return for the ten years of the agreement. Similarly, Hemas' return to the office space rental business with Hemas House, its new office complex, can be seen as another means of investing excess cash in order to be assured of a steady stream of income.

The key challenges for Hemas will be to continue to transform itself and sustain growth on its 5x vision[19]. The CEO, Husein Esufally, has to transform his role through a process of self-renewal as he increasingly delegates key decisions and strives to keep a broadly consensual style of leadership. The CEO articulated the following challenges that need to be met:

1. Becoming the market leader in Personal and Healthcare industries
2. Helping connect Sri Lanka with the world
3. Developing unique leisure experiences.
4. Building an organization that fosters creativity and innovation thus empowering people to fulfill their ambitions

Some of the most important issues facing the company are listed below in summary. Most of these are substantially expanded on in other sections of this commentary.

Sustaining Growth

Hemas will be challenged over the next few years to sustain its growth rate of the past years and to meet its promise to deliver the best ever results of a listed company over its first 7 years of listing. The company is looking to expand its existing business segments, but expects to reach much of its targeted growth through mergers and acquisitions (see Table 1). While Hemas reaffirms its commitment to areas that will provide synergies or economies of scale, it will be under pressure to grow by acquisition to meet its top-line financial goals. One key concern is that Hemas might be tempted into acquisitions or ventures in non-strategic areas for short-term gains. However, the company has shown an ability to correct mistakes and exit promptly from sectors with diminishing prospects. Another concern is that the company is still focused on Sri Lanka, with no real attempt being made to build export markets or go offshore to the Maldives or India. The growth that Hemas has historically managed and seeks to continue will run up against the constraints of a relatively small domestic market in Sri Lanka. It will need to compete more globally to sustain its desired growth.

[19] Increasing the share price to 5 times its IPO value by 2010

Change Management

- *Cultural Change*: Hemas is in the process of managing a transition from a low profile private family business to a modern, publicly listed, investor friendly conglomerate. Hemas must consider the impact of the radical changes in its manner of conducting business and dealing with its staff while maintaining companywide morale.
- *Succession Planning*: At the highest level, much of Hemas' success and vision over the past 15 years has been due to its current capable CEO. Once Husein Esufally leaves his executive position in the company there is no doubt that Hemas will have a huge void to fill. While this need is not immediately pressing it is one for which the company should begin planning now. Hemas in general has not been active in the area of succession planning, which will be an important area for emphasis over the next few years.
- *Creating a Meritocracy*: Hemas is moving from a company of owner/managers to a professionally managed business with a clear separation of management and ownership. While its family directors are themselves professionals, Hemas needs to send out a clear message both internally and externally that it has the Human Resource Development systems in place to track and reward the performance and development of other professionals within its organization. The charting of a growth path for key individuals is essential to demonstrate that a clear future with the company is possible for non-family professionals.
- *Attracting and Retaining Talent:* Hemas compensation packages appear to be comparable with global multinational organizations in Sri Lanka, but training and employee development are also areas that will need higher focus. On the personnel development side, ambitious performance appraisal programs (including 360 º degree ones) are being discussed and should feed into decisions on training for individuals. Training budgets will need to be made more commensurate with the company's aggressive growth plans.

Focusing on Core Competencies

To avoid loss of focus and diversification in too many different directions, a common occurrence among rapidly growing organization, it will be critical that

Hemas establishes clear strategic guidelines for diversification planning and scenario setting. Focus on core competencies must play a large role in guiding new business decisions.

Capturing Corporate Synergies

The company is set up along the lines of a modern corporation, whereby the parent company is intended to provide policy and strategic direction to subsidiaries. However, the separate business sectors appear to function largely as independent companies with services provided by Hemas Holdings being restricted to administrative functions. Hemas Holdings' executive directors perform as functional heads and therefore cannot step back to look at areas that run across all business segments, such as human resources, long term management, strategy and other macro support services by way of strategy or consultancy.

4 Key Findings

4.1 Impact of Government Policy

The 1970's import restriction/export promotion policies had a profound effect on Hemas' lines of business – one that has clearly influenced the diversification seen in the company today. The restrictions on imports and foreign exchange together with the setting up of State Pharmaceuticals Corporation (SPC) effectively stalled Hemas' core Pharmaceutical business. Though private companies had previously supplied pharmaceutical products to hospitals directly, they could now only be made through the SPC by a tender process. Due to its dependence on imports of pharmaceuticals, laboratory equipment and other school supplies, Hemas' overall business activities were severely affected by the new policy changes.

In addition to its core pharmaceutical and import businesses, the Esufally family had supplemental income from its rental properties and tea estates, which was virtually eliminated as a result of the nationalization of the tea estates by the Government of Sri Lanka (GSL) and the passing of the Rent Control act. The combined effect of these policy changes and the recently introduced Wealth Tax, forced them to look at new potential sources of income. As a company, Hemas' strength was its openness to entering new areas of business, stemming from the entrepreneurial spirit of its owners.

In an effort to both support its existing businesses and bolster its earnings, the company chose to enter businesses that were eligible for the Foreign Exchange Earned Credits (FEEC)[20] program and other tax incentives being offered at the time. The GSL focus was on promoting tourism (eligible for preferential tax rates and vehicle import licenses), exports, and other foreign exchange earning ventures. Hemas

[20] Companies earned foreign exchange credits against the value of their exports. Many companies set up export businesses purely to satisfy the foreign exchange needs of their other businesses.

ventured into diverse businesses such as tour operation, hotel management, exports of commodities, gem and jewelry exports, an overseas employment recruitment agency and apparel manufacture for export. Due to the poor performance of its older established businesses, the company was not in a position to make high capital investment.

This period's new business ventures were primarily low capital intensive, foreign exchange earners, a trend that continued through the 1980s. Despite the tax holidays and tax write-offs being offered, Hemas at that time did not enter businesses requiring large capital investments, such as hotels. Much later, nearer to the end of the 1990s the company did invest in some hotel properties and capital-intensive manufacturing businesses. Even today one of the company’s trademark financial features, its high return on investment, is partly due to its policy of being in low capital-intensive businesses.

In the early 1990s Hemas invested in the manufacture of the Baby Cheramy product range and other new products of its Personal Care business. These included toothpaste, shampoo and most recently soap. Hemas was granted pioneering industry status for its Clogard toothpaste. In 1996 Hemas entered the hotel sector with two separate investments through indirect ownership stakes in Serendib Hotels and Mowbray Hotels. The former is a listed company, owning three hotels (Serendib, Hotel Sigiriya and Dolphin) and the latter a development property (Peace Haven) in Tangalle. Later in 2003, Hemas acquired a 47% stake in Associated Hotels which owns Lihiniya Surf for Rs 100 million. Trading income on its hotel investments are subject to a preferential tax rate of 15%.

During the 1990s, taking advantage of Board of Investment (BOI) tax holidays and incentives, Hemas also made a series of other capital investments.

- In 1992, it began apparel manufacture, which was exempt from tax for a 15-year period under the BOI Act. Since the business failed to meet ongoing financial targets, the company sought a strategic partner and partially divested it in 2005, retaining a 30% shareholding

- In 1996, it set up a manufacturing facility for generic drugs, which now makes up 10% of its pharmaceutical sales. This facility received a BOI approval and import duty exemptions on its machinery. In addition, there is a five year tax holiday on income/profits.
- In 1997, it returned to the real-estate business with construction and operation of a BOI approved modern office complex in Colombo 2. The project has a seven-year tax holiday and provides the company with a steady cash flow.

Most recently, in 2003, Hemas received BOI approval for its latest investment, a 100 mega-watt thermal power generation plant. This joint venture provides both a five-year tax holiday on income/profits under the Inland Revenue Act and a ten-year tax exemption from the BOI, followed with a preferential tax rate of 15% on income. This investment has again allowed Hemas to diversify its economic exposure while providing it with a competitive guaranteed return.

4.2 Management Style

The overriding company characteristic is driven by the family entrepreneur heritage and a clear passion for making money. Loyalty is an implicit corporate value. The culture is homogenous and organic, in that it is grown from within. It is easy to identify, never postured or ritualized. We see no symbols and unique rituals of the larger multinationals or textbook corporations that ventured this route. Diversity is not apparent. Mavericks are not seen, nor perhaps encouraged. Mistakes are tolerated, but risk taking not encouraged.

One of the interesting features of the Hemas style is its fine balance of strong leadership and family control, with an ability to absorb inputs from experts, consultants, board members or key directors where necessary. The overriding present management style is defined by the "seemingly laid back but strong sense of direction" approach taken by Husein Esufally who has masterminded and made recent changes possible. He has shown behavioral competencies that need to be studied.

Leadership models are possibly the most important facets that need to be built into Sri Lankan businesses. The spirit of entrepreneurship is helped by cultural environment and socio-ethnic values but it ultimately boils down to a set of characteristics that can be developed and adapted. It is in this context that we attempted a leadership diagnostic of Husein Esufally as the key driving force behind the company's recent successes and its ability to move into the big league.

The diagnostic was performed on competencies of business leadership, commonly acknowledged in existing management and Human Resource theory. The writers attempted to rate CEO Husein Esufally on each individual competency, based on responses of the CEO himself, board members, and employees during the series of interviews. With the exception of "Takes risks", Husein Esufally rated very favorably on the following competencies:

- Takes the long view
- Formulates visions
- Takes risks
- Explores new territory
- Initiates change
- Transforms
- Empowers
- Encourages diversity
- Invokes passion
- Acts morally
- Is accessible
- Is fair
- Is task driven
- Manages the detail
- Is adaptive

In summary CEO Husein Esufally displays high character and a strong authenticity. Corporate leadership is at times one of posture, in which management attributes are cultivated and not consistent, and that is why authenticity is important. It must be noted that this is a young man who as a consequence of the privilege of birth was somewhat cosseted and as a younger sibling was not traditionally the automatic heir to the family business's leadership position. Husein proved himself with performance and earned respect within the family and the business. He rose to the challenges of re-engineering, which in reality he championed and saw through. He had the right mix of ambition, vision, diplomacy, shrewdness, flexibility and perseverance that makes him worthy of leadership and worth studying.

4.3 Shared Values

There is a common acceptance of the dominant value of integrity within the company. Hemas plays fair and straight. They have demonstrated that success can be achieved without being unethical and breaking the rules. For instance while it is generally important to have good dealmakers when obtaining government contracts, there is no doubt that Hemas chose to link up with the best in class strategic partner and won the power project tender fair and square. To a certain extent market reputation is such that the business community knows that it has to be above board in its dealings with Hemas. The company has a track record of exiting potential

Hemas' CEO, Husein Esufally, articulates the old founding values and the new values he hopes to build as follows. We quote verbatim:

Founding values:

1.Honesty & Integrity, 2.Entrepreneurship, 3.Prudence & Conservatism, 4.Trust & Respect 5.Simplicity, 6.Staff part of Hemas family

New values:

1.Commitment to Integrity, 2.Driven by Innovation, 3.Bold in thought, 4.Obsession for Performance, 5.Passion for Customer, 6.Concern for People, 7.Simplicity, 8.Open society, 9.Sense of urgency

It is our view that two of Hemas' primary historical core values, Entrepreneurship and Prudence/Conservatism, are possibly true of most family businesses in Sri Lanka or the world. However the differentiating values such as Trust, Respect, Simplicity, Staff as part of the family, Honest, and Integrity are not as common. In addition, Transparency, Frugality and Disciplined Work Ethic are three characteristics, though not mentioned in the core values by the CEO, which were the key drivers of early success in the first 50 years.

The Company has published a formal statement of the new values. However, these are not consciously invoked in important decisions. The question “will it make money?,” is the single most important hurdle, rather than strategic fit with the current business, etc. Values are introduced to new employees but not ritualized. However a strong awareness and reading of core values of integrity and ethics pervade.

The Company Vision has a time horizon of five years and is purely financial (increase share price 5 times by 2010). On the other hand, the company’s mission is about commitment to exceptional value delivery and the pursuit of excellence. Many in the organization participated in formulating the mission at the annual retreat.

> ***Hemas Mission***
> *We are committed to delivering to our Shareholders the best ever returns a listed Company has given over the first seven years of listing. For our Employees, we are committed to creating exciting new opportunities and a rising share of wealth. For our Business Partners, we will be a winner to grow with. To our Customers, from all quarters, we will deliver excellence... every time. We are a responsible corporate citizen close to the lives of the Community. To the State, we are a future winner with the nation at heart.*

In our evaluation the company values in reality are

- Integrity
- A strong work ethic
- A culture of discipline
- A general guiding principal of simplicity
- Frugality
- Commitment
- Passion about making money
- Passion about the business

4.4 Strategy

When we discuss Strategy, we are looking for a pattern or plan that integrates the organizations' major goals policies and programs into a cohesive whole. A lack of cohesion itself could be a deliberate strategy. Traditional strategy commentaries look for a tidy fit of maximizing relative internal competencies in the strategy adopted. Typically the marshalling of resources is based on where a company wishes to go vis a vis a clear understanding of the category and environmental risks and opportunities. We have endeavored to use strategic commentary right across this study and have also looked at some standard tools - for instance the SWOT analyses and the *Porters Five Forces*[21] model - in analyzing specific SBU case studies. We have also suggested some steps the company could take, using a S*corecard* approach, to managing excellence by tracking initiatives in a globally accepted template (EFQM model[22]) and have made an indicative placement of where they may possibly be in this context right now. By measure of hindsight, Hemas has been exceptionally successful.

Management studies generally agree that three consistent values amongst successful companies are operational excellence, customer intimacy and product leadership. Broadly speaking Hemas scores high on all these. They are currently focused on unleashing and creating shareholder value and believe the best route is by making strategic acquisitions to sustain the pace. They are open to entering new areas at a pace they were hitherto too risk averse to venture into, especially with heavy capital investments. They have made a cumulative impact of the good market decisions, have known when to exit from bad ones, have built strong relationships with suppliers, principals, distributors and staff, which along with marketing savvy is one of their strongest characteristic. However the transition to a fully professionally managed business is incomplete, as it is still family controlled and managed. They seem to have occasionally explored future scenarios, but are possibly at an opportune moment in their evolution for an extensive scenario scanning, soul-searching exercise.

One strategy gap seems to be in Human Resource development and again we suggest it needs prioritizing and perhaps closer monitoring by the main board. Company

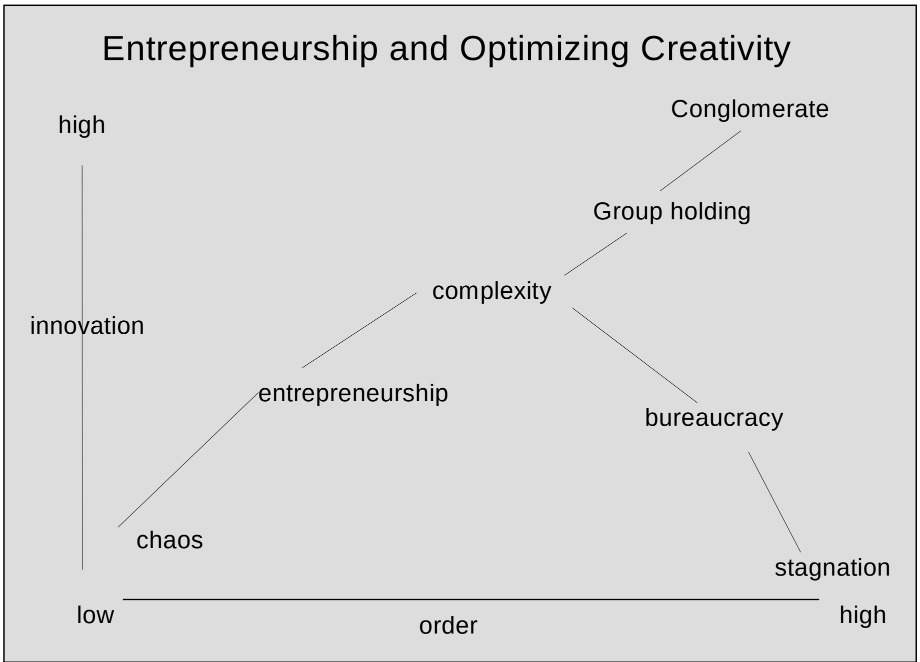
[21] Michael E. Porter: *Competitive Strategy* – Techniques for Analyzing Industries and Competitors
[22] European Foundation for Quality Management

performance is largely influenced by the kinds of management practices that are adopted by the company.

4.5 Workforce Development

The EFQM, presented later on, critiques the capacity for people development and involvement as being ones that the company must now focus on. (See concepts 5 and 6 of the EFQM matrix below). The company in the past was far better at workforce development despite the fact that it was much less concerned with reward mechanisms. Then the company was run with paternalistic management style that was successful for that era, as it had a "work for life" policy. However, as the world changes and work pressures are greater and competency levels are in demand from competitors the company is making attempts to move toward performance linked compensation and good industrial relations. In order to deliver its ambitions growth forecasts, the company must place much more emphasis on performance based rewards and evaluations and a allocate a larger (at least 5 times) amount of funds to fuel its manpower development needs.

Figure 17 - Entrepreneurship and Optimizing Creativity



From SME to conglomerate, optimizing innovation through managing complexity

When small family owned and run businesses that were in command and control mode, grow in size, they need to implement the relevant structures and systems to deal with greater complexity. The challenge is to retain some characteristics of flexibility, and to delegate, empower, and unleash the creativity and innovation, that enabled it to outwit larger competitors. While Hemas has addressed the issues of organizational structure and is moving towards a conglomerate structure, it still has a lot to do in the area of HR to manage the process. Largeness creates impersonal administrative structures that are the antithesis of a business that had an ethos of community.

To minimize the inevitable employee insecurity resulting from the distance between senior managers and employees, created by a Holding Company structure, Hemas should maintain a high level of communication through the organization, emphasise employee development, allocate sufficient time/money on training, and continue its tradition of celebrating the tenure of long term (25 year) employees.

The Deloitte Human Capital Management Value Map is highly recommended as a tool that can clearly articulate the strategic value HR brings to an organization. It tries to bring a highly structured *Scorecard* approach to managing change and helps a company do what they do better and change what doesn't fit, in a change and growth contexts. Seven human capital strategic values are tracked of a list of some 400 initiatives. The value map could possibly be used as the basis for ideas brainstorming on what sort of initiatives might work in the Hemas and Sri Lankan context.

4.6 Management Information Systems

In this section, rather than provide a comprehensive description of Hemas information systems, we instead highlight two key applications that illustrate the company's use of world-class Information Technology, in order to achieve a competitive edge.

4.6.1 Automated Order Entry and Inventory Management

A recent completion of a distributor direct sales computerization program has paid dividends and given Hemas an edge over the competition. Despite some hiccups in implementation, handheld computers have been provided to sales reps for order entry in the field, which are later transmitted over fixed lines for order processing and fulfillment. In addition a strong inventory control system has been put in place. This will stand the company in good stead as distributorship plays a critical role in market success.

4.6.2 SAP

Founded in Germany, SAP is among the top five software companies in the world and the vendor of the Enterprise Resource Planning (ERP) software program that bears its name. An ERP program is essentially a transaction management system rather than an optimization tool. It attempts to integrate all the different departments and functions across a company onto a single computer system that services each department's particular reporting and information needs. If implemented correctly, the integrated approach can have significant payback.

Since ERP systems require strict adherence to process, implementing SAP offers an opportunity to streamline the business processes in an organization. Typical benefits of an ERP system are; a) easy access and visibility to common information by all the various departments, which eliminates duplicate data entry and improves data accuracy; b) standardization of data and processes across the organization; and c) better co-ordination across different departments, due to improved communication and information sharing.

Hemas is investing Rs 120 million (US$1.2 million) with recurrent annual support costs of around Rs 30 million (US$ 300k), not counting any additional development expenses, to implement SAP across its organizations. The company has recruited an expatriate to be the Director of Information Technology, with the specific responsibility of guiding the company's SAP implementation.

The primary goal established by Hemas for its SAP program is "the establishment of common processes across each business sector". This includes implementing the best practices in the FMCG and Pharmaceutical industries that are supported by SAP. In addition SAP will be used to support the company's Shared Services unit with the processing of payables and payments across all businesses. Other benefits that Hemas is looking for are improved order management (entry, accuracy, tracking, cycle time/speed), sales forecasting, and inventory management.

The common challenge faced by companies implementing SAP is that it requires them to change the way they work, and people don't like to change. In fact the software is less important than the re-designed business processes and simply installing it without process change may yield limited results. It is important that Hemas senior management does not underestimate the importance of being committed to and/or training their workforce on their new business processes.

4.7 Corporate Social Responsibility

In early 2002 Hemas commenced a focused community response program directed at Early Childhood Care and Development (ECCD). Though the program was initially developed with UNICEF, it began with the company's market interest in the baby product category and their flagship brand Cheramy and was called *Piyawara* (which means footsteps). However this had limited impact and in 2003 the company moved away from the UNICEF tie-in and reinvigorated it on their own as a stand alone CSR project. It was re-designed in collaboration with the Ministry of Social Welfare children's secretariat and was built on a desire to give back to the community in the form of a comprehensive child focused project.

Such programs are typically used by corporations for constant promotion and brand infiltration and run by outsourced brand building companies. These program are usually expensed out as brand promotions and run by brand management teams. The bulk of the cost incurred is for promotional hype rather than any real societal impact. In the case of Hemas, it is important to note that in keeping with the company's core value of "integrity" this project was not viewed as a strategic brand hype activity or a CSR exercise to gain mileage for the brand, but instead became a project that was passionately driven by Shiromi Masakorala and firmly rooted in and of the societal need.

Piyawara now is an entire integrated educational program that contributes to the capacity building of the government educational system. Thirteen permanent schools have been upgraded with three regional centers of excellence. Some of the work done in this program has been truly ground breaking. The regional centre in Jaffna was the country's first preschool in the north, starting off in a small garage space in the municipality. It was no mean task to be able to win the support of the rebel controlled policy systems and the government hierarchies to get this off the ground - to start from scratch and find/train teachers - as a system did not exist. The approach from the beginning was not about tokenism but one of creating a centre of excellence and getting a job well done.

The impact to the community in the early period of the post peace treaty era cannot be overstated. All three regional centers of excellence in Polonnaruwa, Matale and Jaffna can all claim to be resounding successes. The program does not merely build bricks and mortar but has developed a holistic approach to teacher training and parental awareness generation. It is community centered and managed and has succeeded in training 100 teachers per district. The schools committee is represented by the parent teacher association, the secretary local government and also individual parents and teachers. These committees are being empowered to manage the schools and raise funds. A three party MOU, between the local government the ministry and Hemas governs administrative issues.

After the devastating tsunami of December 26th, which destroyed the livelihoods of a half a million plus people and US$900[23] million in assets in the coastal areas of Sri Lanka, several private sector groups were actively involved in tsunami relief. Hemas was prominent among them. The *Piyawara* program addressed the impact in areas such as education, trauma counseling and housing. It must be noted that a total of 182 schools, 4 universities and 15 vocational training centers were damaged. Children and women were the most vulnerable groups.

Hemas early intervention in the transitional preschool area provided tremendous systemic support. A Hemas Tsunami Trust Foundation was founded and 27 temporary pre-schools, which were set up in refugee camps after a quick needs survey, were operational within a month of the tsunami and catered to 2000 children. Hemas has committed to providing teacher salaries for these transitional schools for the first year. These schools, which were set up so that the care and education of the children was supported in a period of total chaos, greatly facilitated the capacity to get children back to some state of normalcy in their lives. Special trauma counseling support was also provided for. Further, twenty new state of the art pre-schools at a cost of LKR 5.5 million (US $55,000) each with creative play and trauma counseling

[23] Report by TAFREN (Task Force for Rebuilding the Nation)

facilities are being built. Ten will be fully operational by the end of the first year (2005). Most of the funding has been through Hemas and its business partners. ADB too has been involved in two schools.

It must be noted that the building of schools in the short period after the tsunami where land allocation issues were a deterrent to the most fervent of donors is a particularly tremendous achievement. Ms Masakorala has amazing personal zeal, commitment and perseverance - going from pillar to post and bureaucrat to bureaucrat to gain the necessary approvals. Anyone who is familiar with the constraints within the system can truly be amazed at the efficiency and speed of implementation of this program. Again with no huge infrastructure or support within or outsourced Hemas has shown that commitment, empowerment and a passion to get a job complete can work. Most other large multilateral INGO and Corporate entities are still struggling to get to base one on tsunami reconstruction.

5 Benchmarking and Analysis

5.1 Comparison with Similar Previous Studies

We will begin our analysis based on a comparative survey of attributes associated with business success as per four critical and relevant management studies on successful business practices both in the Sri Lankan context and in the regional and global context. We use these to look for similar attributes in the Hemas business. The studies are chosen based on the following rationale. The first study is the only real Sri Lankan business benchmarking study, the second and third are well known American studies that have used the detailed analysis of a historic evolution of companies in an approach allied with ours, the fourth is a East Asian regional study.

Study 1: In June 1999 the Post Graduate Institute of Management (PGIM) Jayawardenepura Sri Lanka conducted a research study of 40 large and successful companies in Sri Lanka, in which a group of researchers surveyed the current management practices and how they contributed to company performance, looking at: 1) long term client relationships; 2) equity and consideration in managing people: 3) a growing passion for quality: 4) results-based controls; and 5) task before structure.

Hemas Assessment: All these characteristics are present in Hemas, to a lesser or greater extent as stated values within the company. As the previous study methodology (PGIM) was more response-based than observational, they still hold. However as this is a more detailed study there is a difference in analysis

1. Long-term relationships with partners and suppliers are a key factor for success. However we use an EFQM model further down to chart some scope for Hemas building customer intimacy and ingraining it into planning methodologies as a possible strategy for sustaining competitor advantage and growth. The Personal care division of the business built tremendous market

success through being able to take on key multinational competitor Unilever, partly by finding opportunity gaps in the markets and producing culturally relevant communication and products positioned for this. Clogard, Baby Cheramy and Komarika are classic examples of Hemas' immense capacity to build strong brands. In the case of Baby Cheramy - quality and trust were the consumer insights as category drivers, and thus a more international identity was developed to take Pears Baby head on, whilst in the other two cases, localized and herbal/indigenous traditions were used brilliantly, to win a share of over a third of the market..

2. Equity and consideration of people, critical features of how Hemas built its success, are areas in which the company must continue to maintain focus.
3. Quality is not necessarily a passion, though the company has it as a management concept..
4. Results-based controls are strong and tracked well, and definitely contribute to success. The computerization of the distributor networks has helped tremendously and SAP will further enhance this, once fully developed. .
5. Task before structure is also preferred except when the company decided to go public as this was recognized as being the key barrier to doing so.

Study 2: Collins and Porras[24] *Built to Last: Successful Habits of Visionary Companies* © 1994) is the result of a six-year study of the underlying factors that contribute to the success of visionary companies. Collins and Porras define visionary companies as those that are widely admired industry leaders with a long-term track record of having a significant impact on the environment. They examine their core ideologies and present a framework that demonstrates how visionary companies stimulate progress while preserving their core ideologies. Their sample comprised of 18 companies, most of them American. The companies in the study were, 3M, American Express, Boeing, Citicorp, Ford, General Electric, Hewlett-Packard, IBM, Johnson & Johnson, Marriott, Merck, Motorola, Nordstrom, Philip Morris, Procter & Gamble, Sony, Wal-Mart and Walt Disney. However, their methodology was unique

[24] The author James C. Collins is a management educator who has taught previously at Stanford Business School. He has also worked with McKinsey & Company. He is the co-author of *Beyond Entrepreneurship* and *Managing the Small to Mid-sized Company,* and Jerry I. Porras is a chaired Professor of Organizational Behavior at Stanford Business School. He has worked previously with General Electric and Lockheed. He is the author of *Stream Analysis* and *Good to Great*.

in the sense that they examined the entire history of each company in the sample - no mean feat. Our attempted methodology as a single case study uses the same approach of tracing the historical evolution of a company's success over a long period of time.

Their objective was to discover 'timeless management principles'. The key components of these principles, as they discovered, are:

1. Becoming a clock builder, not a time teller
2. Choosing A and B rather than A or B - try a lot of stuff and keep what works
3. Preserving the core and stimulating progress
4. Seeking consistent alignment.
5. BHAGs (Big Hairy Audacious Goals)
6. Cult-like Cultures
7. Home-grown Management
8. Good Enough Never is

<u>Hemas Assessment</u>

Again it is necessary to note the parallels and the departures.

1. Other than for the Power Project, Hemas has certainly been a clock builder in its approach. The Power Project was unique in that it was a passive and strategic investment of excess cash and a leap from the risk-averse, no-high-capital-investment approach to a risk-free, guaranteed-return project.
2. They are now moving into a *try A and B* approach of multi-pronged growth strategies. Hemas has a strong capacity to exit and push out bad investments and retain the good.
3. Preserving the core - this seems to be an issue if the company will lose some focus. But success to date has been from core competencies and categories
4. Seeking consistent alignment - not observable and linked to the lack of focus issue raised earlier.
5. As the company now chases its first truly BHA goal - the 5X vision - a strategic openness to diversify on many fronts across all divisions is noticed
6. It is interesting to also note that Hemas had a cult like culture, even though it was never overt or ritualized, that is now being replaced by an amorphous cosmopolitan one. Some thought on keeping an identity through stronger HR and internal communication will be key.

7. Homegrown management is a key feature. (We refer to this as homogenous and organic in the culture review section). The need to spend more money on people development becomes increasingly relevant. We must note however that a mix of external inputs from key professionals and consultants at the right time as well as strong inputs from external board members have also helped the company at critical turning points. Some of these external influences have included: USAID consultants just prior to restructuring, Mr. Tilak Pathmarajadasa - a management accountant formally with Ernst and Young, Mr. Lalith de Mel- one of the country's veteran marketers and the only Sri Lankan placed on a main board of an Anglo-Dutch multinational Reckitt Benckiser, and Hilmy Cader - a Bahrain based Sri Lankan management consultant.
8. "Good is never enough"- The ambitious goal setting and continuous capacity to stretch, manifest themselves as comparable characteristics. The company is neither complacent nor sits on its laurels.

Study 3: Jim Collins, in his book *Good to Great* (Harper-Collins, 2001), examines 28 American companies between the years of 1965-1995 to find out how some companies and not others make the leap to become great. He describes his findings as follows:

1. Great leaders are self-effacing, quiet reserved, even shy
2. Get the right people on the bus, the wrong people off and the right people in the right seats
3. Confront the Brutal Facts (Yet Never Lose Faith). Maintain unwavering faith that you can and will prevail in the end, regardless of the difficulties, AND at the same time have the discipline to confront the most brutal facts of your current reality.
4. Be the best in whatever core business
5. Have a culture of discipline and combine it with a culture of entrepreneurship
6. Becoming great is a relentless process, not a dramatic change program

<u>Hemas Assessment:</u> When viewed against Collins' findings, Hemas and the Esufally family are seen to demonstrate many of the traits required for a successful business.

1. They provide self-effacing, reserved, yet strong leadership to their employees.

2. They make an effort to get the right people (their family members fully committed to the business, with business instincts and company loyalty instilled in them from childhood) into the business
3. They believe in their ability to prevail in the end, but are able to take a clear look at their situation in times of business difficulty
4. They constantly strive for excellence by trying to do better than and prove themselves to the previous generation that bequeathed to them, or oversee them in, the family business.
5. They have a strong personal culture of discipline, while being highly entrepreneurial in thinking
6. They are willing to adapt, investigate new areas and lines of business, including technology. They are willing to engage in business as a continuously evolving process

Study 4: Halim (1998) examined 95 companies from six Southeast Asian countries (Hong Kong, Indonesia, the Philippines, Thailand, and Singapore). These companies were compared to over 600 other companies and multinational corporations operating in these countries. The key attributes of the Asia's best included:

1. In-house facilities for world-class training of their employees
2. Providing and communicating value to customers
3. Concentrating on core competence and a set of operational activities
4. Managing alliances and joint ventures
5. Competing for the future

Hemas Assessment:

1. Training is a feature that should be, the single most important area of concentration for the company as it moves to the next level.
2. Hemas does provide and communicate value to its customers
3. Concentrating on core competencies are present and strong mainly in the personal care and healthcare division. However the core principle of making money could override the competency-based approach, which often leads to a lack of strategic focus/intent.

4. The last two attributes are emerging as strong features of the current business and the capacity to managing alliances and joint ventures and partnership may well be their strongest competency. (See EFQ Matrix)

5.2 Operational Excellence/EFQM Template

This section analyzes the company against the European Foundation for Quality Management (EFQM) template of classic concepts for corporate excellence. It must be noted that this is an indicative assessment, as a full-fledged one requires a far more extensive list of questions and the consultation services of a certified assessor for proper validation. It is recommended that Hemas explore such an activity.

This Model, which is the application of the Fundamental Concepts reflected in a structured management system, is now being used by tens of thousands of organizations in the west, including companies, schools, healthcare organizations, police services, utilities and government offices. The Model additionally provides these organizations with a common management language and tool, thus facilitating the sharing of 'good practice' across different sectors. It is hoped this will assist the company improve its performance in the basis of these yardsticks. The EFQM Excellence Model is often used as the primary framework for assessing and improving international competitive organizations, and tracking world class approaches of management that would lead to sustainable advantage.

The EFQM premise is "*Excellence is not a theory; it relates to the tangible achievements of an organization in what it does, how it does it, the results it gets and the confidence that these results will be sustained in the future. The evidence needed to give that confidence is not limited to the financial results, which demonstrate the outcome of past performance. The evidence also includes results from other stakeholders that serve as leading indicators of future financial performance. These leading indicators include, measured excellence in customer satisfaction and loyalty; people motivation and capability; and the satisfaction of the wider community. To create confidence that the results can be sustained, there must also be evidence that what the organization does, and how it does it, is soundly based, systematic, and continuously reviewed and improved."*

In summary the purpose of this analysis would be to assess the company's standing in an international context. Using a well-known and widely accepted model, eight key characteristics are tracked. The following table contains the broad definitions of the eight concepts and the different levels of excellence that the company is measured against.

Table 2 – EFQM Performance Matrix

Characteristic	***Concept***	***Levels of Excellence***		
	Excellence Is….	**1. Startup**	**2. On the way**	**3. Mature**
1. Result orientation	Achieving results that delight all the organization's stakeholders.	All relevant stake holders identified	Stake holders needs are assessed in structured way	Transparent mechanism exists to balance stake-holders expectations.
2. Customer focus	Creating sustainable customer value.	Customer satisfaction is assessed	Goals & targets are linked to customer needs & expectations. Loyalty issues are researched	Business driven by customer satisfaction needs & loyalty issues understood, measured & acted on.
3. Leadership and constancy of purpose	Visionary and inspirational leadership coupled with constancy of purpose.	Visions & missions are defined	Policy, people & processes are aligned & leadership model exists	Shared values and ethical role model exist at all organizational levels.
4. Management by processes & facts	Managing the organization through a set of interdependent and interrelated facts, systems, and processes.	Processes to achieve desired results are defined	Comparative date and information is used to set challenging goals	Process capitalization fully understood & used to drive performance improvement
5. People development & involvement	Maximizing the contribution of employees through their development and involvement.	People accept ownership & responsibility to solve problems	People are innovative & creative in furthering organizational objectives	People are empowered to act & openly share knowledge & experience

Characteristic	*Concept*	*Levels of Excellence*		
	Excellence Is….	**1. Startup**	**2. On the way**	**3. Mature**
6. Continuous learning innovation & improvement	Challenging the status quo and effecting change by utilizing learning to create innovation and improvement opportunities.	Improvements, opportunities are identified and acted on	Continuous improvement is an accepted objective for each individual	Successful innovation & improvement is wide spread and integrated
7. Partnership development	Developing and maintaining value adding partnerships	A process exist for electing & managing suppliers	Supplier improvement & achievement are recognized and key external partners are identified.	The organization & its key partners and independent plans & policy are co-developed on the basis of shared knowledge
8. Corporate social responsibility	Exceeding the minimum regulatory framework in which the organization operates and to strive to understand and respond to the expectations of their stakeholders in society	Legal & regulatory requirements are understood and met.	There is active involvement in society	The societal expectations are measured and acted on.

The following table lays out an attempt at a high level assessment of Hemas levels of excellence against the eight different characteristics outlined in the EFQM Matrix.

Table 3 - Hemas EFQM Performance Evaluation

Characteristic	*Level of Excellence*	*Observations*
Results Orientation	Level 3	Stakeholder needs are assessed in a structured way, and project based Key Performance Indicators (KPI) are in place. The next evolution is to the level of a mature company with clear performance based evaluation.

Characteristic	***Level of Excellence***	***Observations***
Customer focus	Level 1-2	Like most leading marketing companies in Sri Lanka, customer insight studies are used to establish some degree of NPD and communication. However, customer satisfaction must be continuously measured and goals and targets correlated to customer needs. Given the company's strength in the personal care segment, it would be interesting to see it evolve to marketing plans and budgets that are linked to customer retention or growth
Leadership and Constancy of Purpose	Level 2-3	Strong leadership model exists. Policy, new business and processes aligned to core values of a strong work ethic and "making money". Core competency of marketing and being nimble, agile and relatively fast are harnessed. Leadership issues of succession in SBU's are unclear and not identified. Family members still run key business units. The CEO is the only one of the 4 family members to have demonstrated clear delegation (he delegated the personal care division to a top industry professional). Pharmaceutical and Travel GSA divisions too are run by industry professionals, but other SBU's under family leadership need a delegation plan to be implemented.
Management by process and facts	Level 2	Processes to achieve desired goals are defined and KPI's in place to monitor key systems changes i.e SAP introduction. Comprehensive market plans, feasibilities and documentation in place for project tracking. Next steps are to relate this to performance incentives and a remuneration committee has been set up. CEO and other 3 family members are paid the same package, which is now being unbundled. In view of the inherent turf issues and infighting that often occur in family businesses, this is the best possible route to create stability in a pre IPO era. The company now needs to apply strategic intent and move to greater comparative data to challenge goals.

Characteristic	*Level of Excellence*	*Observations*
People development and involvement	Level 1	While people do accept ownership and responsibility to solve problems or achieve goals, probably stemming from strong personal work ethic, “old world” values of “work for the satisfaction of a job well done” not for incentive or reward, there is opportunity to increase emphasis on exposure, training and remuneration. In addition, a mechanism for people to build creative and innovative pursuit of company objectives and challenges would be beneficial. Change management issues, and ability to attract, retain and unleash potential of best people skills in the market is key, to future growth and sustainability.
Conscious learning, innovation and improvement	Level 1	Though opportunities for improvement are currently identified and pursued, continuous improvement should be institutionalized as a key performance objective for employees. While technology solutions in knowledge management are very high compared to the competition, implementing a mechanism to track or build innovation as a driver is required. Product development and diversification is driven by business opportunity, ease of entry, and potential to make money rather than strategic planning. Differentiation is less important than clever copying. While huge potential to build local market edge exists, there is a tendency to go with the trend of *Indianization* of the Sri Lankan Market.
Partnership development	Level 2	The Company built its early successes based on good contacts, network of partners, and trust based relationships, which has brought in more business in the Pharmaceutical and Transportation sector (GSA’s) etc. The Proctor & Gamble relationship developed into a conflict of interest situation and was terminated. P&G could possibly leverage more from this past relationship, through Hemas contact network.

Characteristic	*Level of Excellence*	*Observations*
Partnership development (continued…)		While some strategic attempt is made in pharmaceuticals for mapping partnerships and opportunities, there is greater opportunity to develop strategic partnerships in the spirit of Lakdhanavi - best-in-class partnerships that are interdependent. The apparel sector, which was performing poorly, was turned around as soon as a category specialist was partnered.
Corporate Social Responsibility	Level 3	Company has moved beyond being compliant to exceeding the minimum regulatory framework in which the organization operates. It has a highly ethical approach to being transparent and accountable to their shareholders. The ECCD early child care and development *Piyawara* project is a huge undertaking executed with an integrated holistic community approach that is a benchmark for Corporations to study. The small administrative structure and understated branding synergies show corporate accountability of a high ethical nature rare in the corporate world. The creation of a knowledge-network in the Pharmaceutical industry and building houses for tsunami victims also need to be commended. Hemas also possibly needs to first focus on the immediate family - its employees. An ESOP more widely shared and executive housing are some suggestions from longstanding employees who see themselves as somewhat left in the cold as the company moves to a meritocracy from a work-for-life loyalty based employment system. Opportunities are immense too if Hemas goes into outsourced government healthcare – (the hospital sector) as part of its redefined category boundaries of involvement.

5.3 SWOT Analysis

A SWOT analysis is an assessment of an organization's Strengths and Weaknesses (usually internal factors) and the Opportunities and Threats faced by it (usually external factors). The following tables are attempts at SWOT analyses of both Hemas Holdings and the Hemas Personal Care business.

5.3.1 Hemas Holdings

Strengths • Strong market repute • Extensive distribution network • Aggressive growth plans across sectors • Money/capital market access to fuel growth • Willing to take greater risk and spend on new market entries • Committed to acquisition and strategic alliances initiatives • Making the capital investment leap	**Weaknesses** • Human capital management and development • Lack of distinctive recent market wins in FMCG – similar to Clogard. • Possibly losing focus of core businesses (taking their eye off the ball) • Value-based rather than competency-based expansion at times.
Opportunities • Tremendous growth gap in all sectors they are in • Healthcare - diagnostics outsourcing from Singapore • Outsourced health services and hospital management for GSL. • Investing in Hotel sector/ finding strategic partners • Mergers and acquisitions-buying leading biscuits or similar top foods retailer • Buying out Wonderlight laundry powder or Khomba herbal soap • Developing strong export capabilities personal care • Investing in ports and shipping	**Threats** • Complacency • Losing key employees • Aggressive competition • Ethnic conflict increasing • Leftwing economic policies • Social unrest • Tsunami

5.3.2 Personal Care Business

Strengths	**Weaknesses**
• Nimble player, able to cater to local environment • Very motivated sales force and product development team • Adept at identifying and filling gaps in local market (e.g. Clogard)	• Lacks economies of scale • Product diversification not strategic • Lack of overarching strategic plans • Potential loss of focus on core brands due to new product emphasis • Losing differentiation with recent price driven entries • Eroding margins • Cash cows milked and not growing adequately?
Opportunities • Increase focus on core brands. • Expand into snack foods and confectionary • Differentiate with more herbal products like Komarika and Clogard • Acquire biscuit or milk food business - huge market segments • Develop export capabilities	**Threats** • "Indianization" of Sri Lankan market • Entry of other multinationals

6 Competitiveness Example

A classic view of competitive behavior is to compare it to war strategies of military greats such as Alexander, Napoleon and Frederick the Great. Carl Von Clausewitz[25] expounded on the paramount importance of clear objectives or targets. Husein Esufally felt the early success of Hemas in the Personal care business was due to its ability to clearly identify the enemy and focus the spirit and thrill of the fight on wins gained.

Interestingly, Clausewitz's central characteristics, spirit, morale, surprise, cunning, concentration in space dominance in selected positions, use of strategic reserves unification over time, tension, and release, are all utilized by Hemas against Unilever. One that stands apart is its nimbleness against a slothful multinational encumbered by category regional directives and the inability to respond at the level of the product with small market specific strategies. A clear understanding of the terrain (consumer insights) was the competitive edge.

6.1 The Clogard Toothpaste Story

Clogard was a tremendous success for Hemas. Not only was it a local brand but it was the local underdog fighting the multinational giant. This became the David and Goliath case history that was the toast of marketing fraternity. Further it made trade partners look up with respect and secret pride. Unilever was the big boy leveraging its market weight to squeeze suppliers and demand retail standards on credit and bank guarantees etc that left the trade wishing for a counterpoint player to help them negotiate. Hemas was to play this role and this industry context gave them much empathy and support in trade entry across all its brands.

[25] Carl Von Clausewitz (1780 – 1831): Prussian general and author of "On War"

Hemas received significant help, on product formulation, from two sources - a consultant funded by USAID and the equipment supplier. A second hand toothpaste machine being sold off by Lankem a paint manufacturer helped them with the cost and decision to enter this market. Storage vessels were designed by Hemas staff and manufactured locally. Product entry and development was carried out over several years.

Hemas decided to stay with Fluoride as a base, rather than grapple with industry standards and classifications. Unilever would have had great comfort if Hemas stayed in the completely herbal grid like "Siddhalepa" and "Supiriviky" two other local brands. However as they produced a *Best-of-East-and-West* positioning they were able to deliver a consumer taste need, linked to a trend in Asian market taste segments (For instance brands such as Promise in India and Darlie in East Asia that catered for a "hot" taste as opposed to the cool mint taste of most freshness toothpastes). In its multiple promises Clogard also offered the antiseptic qualities of Clove, which took it onto a therapeutic value proposition as well as the taste/freshness proposition. Clove was known in Sri Lanka and Asia for its medicinal germ kill properties. (Unilever and the medical lobby refuted the claim stating that the germ kill property could not be substantiated and that it was only a sensitizer).

Hemas initially allocated an advertising budget that was significantly less than that of Unilever, whose aggressive market communication strategies were always superior to its local competitors. *Share Of Voice*[26] was under a third of that of Signal. Hemas had developed a communication campaign that hit directly at Signal, in a comparative ad campaign that was daring for its time, developed by a relatively small local communications company with a maverick underdog spirit, Masters DDB.(small in Sri Lanka but part of the Omnicom group one of the worlds biggest communications groups). It paid off.

Advertising was memorable and distinctive, and Unilever took Hemas to court, on the grounds that the Hemas advertising campaign suggested Signal toothpaste was

[26] Firm's proportion of total promotional expenditure in the market. (i.e - a firms advertising expenditure in a given category versus total category expenditure)

making false claims, Unilever gained a temporary injunction that set the company back by a few weeks but ultimately Unilever lost the court case. Unilever's competitive reaction was the best thing that happened to Clogard as it gave the product free advertising . The verdict also encouraged Hemas to back its product with all its might – allocating 100% of the division's advertising budget to Clogard. It is significant that the decision to stay and fight as opposed to be intimidated and retreat that helped the brand get the full backing that the company may not have otherwise given it. Many commentators, both internal and external, view Hemas as a conservative, risk-averse company. However, this is a clear example of aggressive market behavior that was high risk and perfectly appropriate that worked.

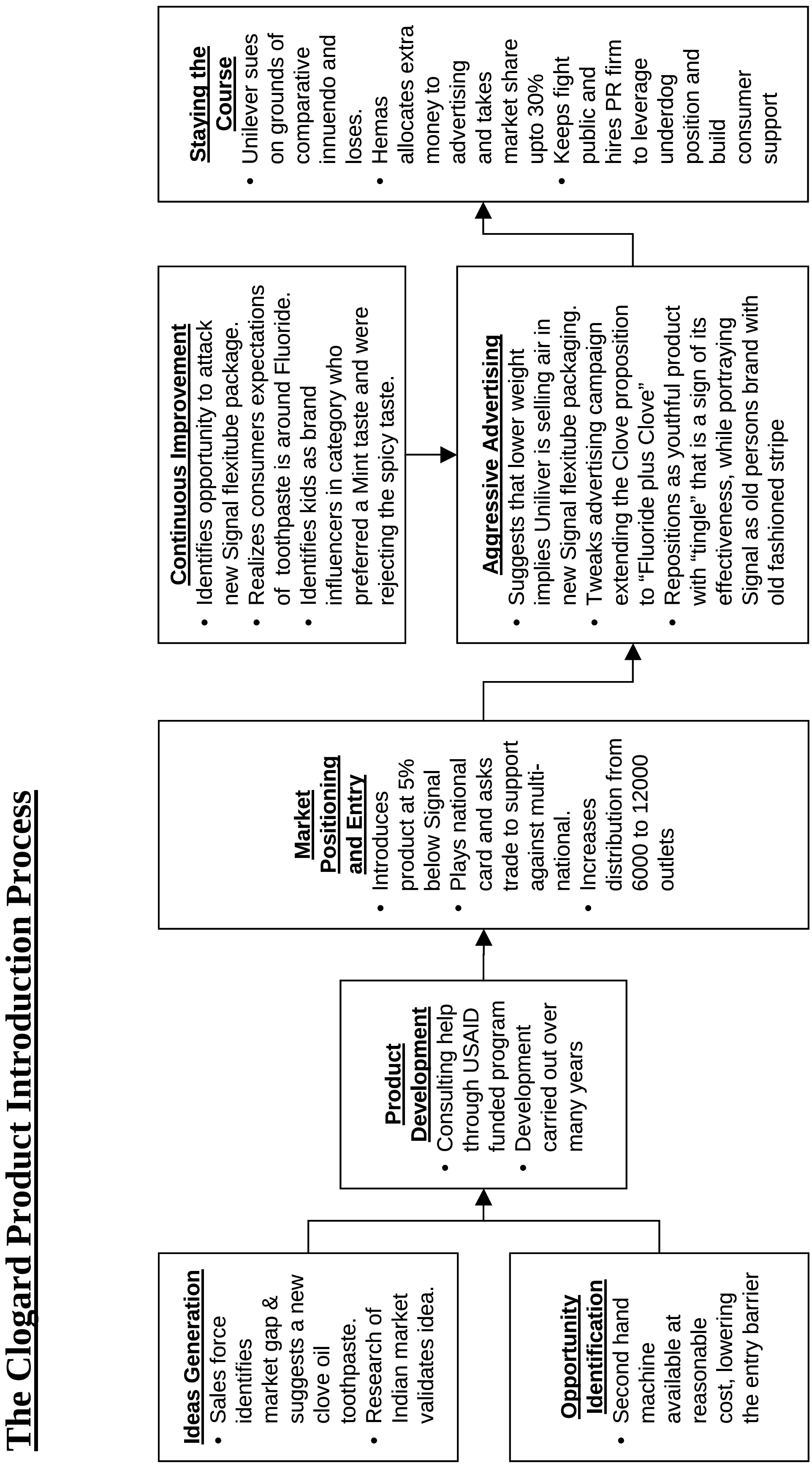
It must be noted that for Sri Lanka and Hemas the entire product technology was new. Almost no company in Sri Lanka without a multi-national partner had R&D and technology support. The CISIR had some basic facilities to product test and ratify formulations. Typically, equipment suppliers were the source of new product technology. Alternatively, new technology was transferred through the recruitment of former Unilever or related experts as consultants or employees.

6.2 The New Product Development (NPD) Process

While the activities described below relate to the specific case of the Clogard product launch and the actions taken by Hemas, it offers an excellent example to illustrate the NPD process of a successful product introduction.

1. *Ideas generation* - This was a classic example of capturing the ideas of employees closest to the market place and consumers. Hemas' sales force indicates that room exists for a new toothpaste entry as market category was large but product choice was limited, and suggests cultural relevance of a clove oil toothpaste. Hemas' study of Indian product Promise suggests opportunity for similar product to be launched in Sri Lanka..
2. *Opportunity Identification* - A second hand machine at affordable price becomes available for purchase, lowering the entry barrier and financial risk factor.
3. *Product Development* - Institutional support and expert advice on technology – a consultant is made available through a USAID funded program.

Figure 18 - Example of New Product Development Process



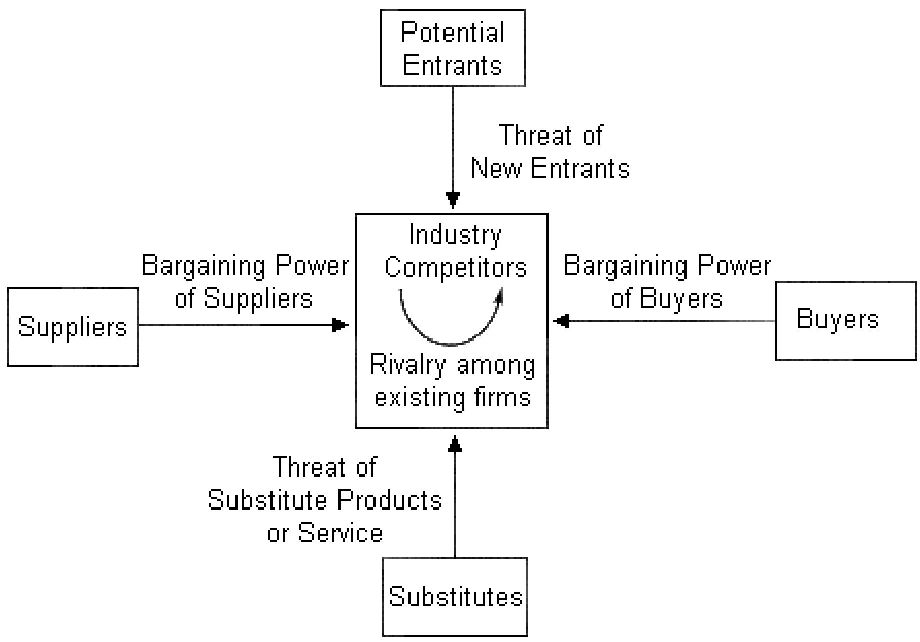
4. *Market Positioning and Entry* - Phase I single minded proposition. New clove oil toothpaste for germ kill enters market at 5 % below Unilever's Signal toothpaste, offering a basis for trail and conversion. Product offers localized proposition from a local company that asks trade to support them against multinational. Company plays national card to achieve market switch at retail trade level.
5. *Widening Distribution* - Leverages product to build distribution and retail presence for company. Moves direct distribution from 6000 to 12000 outlets.
6. *Continuous Improvement* - Hemas closely monitors market response and tweaks advertising campaign, extending the original clove proposition to "Fluoride plus Clove" (bringing reassurance that there was fluoride too) - Demonstrates clear understanding that the consumer's familiarity with the toothpaste category was defined by Fluoride.
7. *Turning weaknesses into strengths* - Unilever upgrades packaging from Aluminium tube to flexi-tube in keeping with the Unilever/Signal global brand strategy to shift to flexi-tubes. To accommodate higher formulation cost and still maintain margins, Unilever reduces the grams/tube, which turns out to be a costly mistake. In addition, there was more air in the flexi-tube, which created consumer mistrust. Hemas communicates the difference as a strength, inferring that Unilever was selling air and brings public attention to the lower weight. Ultimately, Hemas demonstrates communication dexterity and nimbleness whereby it was able to change a technology weakness into a strength.
8. *Aggressive Advertising* - Discovers importance of kids as brand influencers in the category and that kids were rejecting the spicy taste. Identifies that kids don't like product mainly due to a preference for a Mint taste. Uses reverse psychology approach on kids in a brilliantly aggressive comparative advertising campaign that pushes but never oversteps comparative advertising standards. Attacks Signal on its key marker drivers – product taste and the red stripe, once again attempting to make a weakness a strength Repositions Clogard as the product which is modern and has a "tingle" (the hot taste) as a sign of effectiveness. Projects Signal as an old persons brand with no "tingle" and an old fashioned stripe, putting fun and a sense of adventure as kids discover the hot tingle of efficacy. This was a brilliant, relevant and yet simple twist to the consumer proposition.
9. *Staying the Course* - Unilever objects and gets an injunction to stop Hemas' toothpaste production. Unilever sues Hemas for comparative innuendo – Hemas

claim they offer to tone down. Unilever takes them on and loses. Clogard market share rises to 30 % while Signal plummets from 95% to 65%. Hemas wisely keeps the fight public and hires PR agency to leverage awareness of local underdog position and build empathy for consumer support - keeps brand visibility high.

6.3 Clogard's strategy in context of Porter's Five Forces

Understanding the dynamics of competitors helps establish opportunities and differentiate a business. One of the most respected models to assist with this analysis is Porter's Five Forces Model. This model, created by Michael E. Porter and described in the book "Competitive Strategy: *Techniques for Analyzing Industries and Competitors*", has proven to be a useful tool for both business and marketing-based planning. It identifies five forces that determine the long-run profitability of a market or market segment.

Figure 19 - Porter's Five Forces Model



The following section is an attempt to discuss Hemas' efforts to introduce Clogard and the market situation in the context of the Five areas described in Porter's "Five Forces Model", namely Suppliers, Buyers. Potential Entrants. Substitutes and Market Rivalry. The Five Forces model is used here to make a very simplistic analysis of the context of Hemas in the Toothpaste industry, more as an indicative exercise to tie in some of the existing commentary and for use by students that wish to apply theoretical models to live case studies. As a strategic analysis tool for the company itself, far more specific detail is required for the model to be used effectively.

Suppliers

In small markets where volumes are low multi nationals have global leverage on economies of scale. Characteristically, the Sri Lankan toothpaste market was dominated by Unilever with over 95% market share and thus they had all the leverage power they needed locally.

The best defense in mitigating the power of suppliers is to build win–win relationships with suppliers. This is exactly what Hemas did. At the time of the Clogard launch, there were two suppliers of toothpaste tubes in Sri Lanka. The main supplier was under pressure by Unilever to not supply Hemas and the company was restricted to purchasing from the secondary supplier. Due to concerns over quality issues and to mitigate the potential risk of short supplies and/or Unilever exerting influence on their local supplier, Hemas developed a long term relationship with an Indian supplier of tubes, which has served them well.

Buyers

Being the counterpoint to a monopolistic position of Unilever, coming in with a differentiated product offering, and building a brand instead of trading in a generic entry were all key strategies. Playing the nationalistic card against the multinational company, Hemas was able to leverage retail trade support. Some distributors were afraid to carry Clogard for fear of reprisals from Unilever, but at the same time were looking to support it to erode Unilever's monopolistic position.

On the other hand, taking the concept of buyer as the end customer, in Clogard Hemas had developed a consumer insight that was market relevant and identified a market gap to come up with a key winning strategy.

Potential Entrants

The market was defined by one dominant player. The cost of technology and skills needed to formulate toothpaste prevented small local firms entering the industry.

In the local market context, toothpaste was a relatively complex product. Technical know how was minimal. Unlike the common practice in soap manufacture, outsourcing toothpaste manufacture was not possible. Entering this market category required a business to invest in both a plant and technology, which was a serious financial commitment. The sudden availability of an old machine that could be modified would have helped Hemas with the decision to enter.

Substitution

The lack of competitive choice led to highly conducive opportunity for a serious contender, with a valid consumer proposition grounded in local market tastes, to erode market share from a complacent giant.

Rivalry

In Sri Lanka the monopolistic position of Unilever in the Toothpaste market (Market Share of 95%) led to strong competitive rivalry. Hemas worked through strong communication and brand differentiation, improving product differentiation, and exploiting relationships with suppliers. Shortly after Clogard was on the shelves Unilever launched a court case to keep Clogard out of the market, and on a temporary injunction, kept Clogard out of production for several weeks. But Hemas fought back by allocating 100% of the annual advertising budgets from several other brands to Clogard. A strong PR campaign kept the media on their side. Consumers loved the clove promise and the availability of choice and 30% market share was grabbed from Unilever and sustained.

Above all Clogard constantly improved, learnt market and consumer insights on the run and adapted its market proposition accordingly. This was certainly very difficult for a international brand that was bound by global R&D and brand consistency across markets. There is no doubt if Unilever brought out a clove variant, under Signal earlier it might have stemmed the decline. It took almost 8 years for Signal to respond with a herbal. variant This too was a part of a complete “going green” strategy of several Unilever flagship brands such as Sunlight, Lifebuoy and Signal. A delayed response and perhaps an ultimate panic reaction to a decade of market trends as the herbal segment was the fastest growing segment across most of these categories.

Appendices

A1 - The Borah Community

According to S. Muthiah[27], the Borahs, a community of prosperous Muslim traders known for their business savvy and instinct, first arrived in Sri Lanka in 1831 from the Rann of Kutch in Gujarat, India and set up base initially in Galle, later moving to Colombo. Borah traders with fleets of buggalows (sail boats) brought in goods from several Indian ports. A family oriented community, the Borahs runs their businesses also within a family structure. Typically, brothers run separate business sectors and their sons are introduced early into the family enterprise and each allotted a business to learn, master and then run. Those who succeed are rewarded with more funds for expansion and further businesses. Those less capable remain in the business but are moved to less demanding areas where they can manage tolerably. The growth of the business and the family often precipitates the breakup and division of the business among the various family members. Such breakaways however often have the effect of allowing the individual businesses to grow and expand to their full potential, and change with the times.

Typical of Borah businesses is the fact that all family members within a family business share its rewards equally. Whatever is bought by the business for the family is done for all members equally: whether it is a car, television or appliance, all members receive the same model and quantity. This policy leads to fewer family/business tensions and a genuine sense of belonging to both the business and the family. The instinct for business is one that is prized and nourished both in the work place and in society. The intricacies of business, is a topic that Borah businessmen are passionate about. Conversations at the dinner table will often include

[27] S. Muthiah, *The Indo-Lankans* (Chennai: Nagaraj and Company, 2003), 131-142

business, both their own and that of the community in general. Children are brought up with the belief that hard work and business are what counts in life and the goal of entering and growing the family business is set clearly before them. Younger members in the business often feel they must prove themselves to their elders. Success in the work place goes hand in hand with social success and the success of ones business brings honor and recognition from the community.

Borahs are entrepreneurial, conservative, reserved, live a modest lifestyle and place a high value on honor and ethics. They feel that the business culture is in their genes and have an overriding belief that provided the required hard work is put in they will succeed. They are disciplined and hardworking and motivated by financial success. They are a cosmopolitan community, due to their exposure to family and connections abroad and are frequently able to use these links for business opportunities and expertise. They do not indulge in litigation and instead seek dispute resolution through discussion and the intervention of their high priest. These include business disputes and commercial breakaways within the family. Through an agreed upon division of assets, parties draw lots and walk away with businesses and assets in a manner that allows for amicable future relations within a tightly knit community.

In many ways, the Borahs appear to be a community of contradictions. They are intent on financial success yet also determined that all members of the family must share equitably in the business, in some activity, despite individual competency. They are wealthy, yet loath to ostentatiously demonstrate their wealth. They are extremely business minded yet prepared to take advice on business affairs from a religious leader. They are cosmopolitan and sophisticated in their manner of interacting with the outside world but capable of strict financial discipline. They are clearly conservative in their thinking but highly entrepreneurial and willing to look at new areas for business when required to. They run businesses that are clearly family owned yet are able to inspire their employees to perform for the company as if it were their own.

A2 – An Employee's Story

Until very recently, a kindly feudal culture prevailed at Hemas. Staff from family estates, and later their children, were employed in non-skilled jobs such as lift operators and office boys. There was a clear understanding that the company would reward loyalty and hard work, but that laziness and poor performance would result in dismissal. In this model mixed with clear lines of discipline, familiarity did not breed contempt or complacency but instead it was the motivator that was the bedrock that defined the employee's worldview. So much so that to this date a few early retainers still start their day with a blessing ritual to the founders portrait before setting forth to work.

Vellaran (Velu) was brought down from Stafford the Esufally's tea estate in Nuwara Eliya to work for Hemas' founder, Sheik Hasannally Esufally in 1965 as a houseboy in the Esufally family home located on Galle Road in Bambalapitiya. He shifted along with the family to their new house on Flower Road, where he married in 1973 with the support of the family and continued to reside at the family home with his wife and children. Velu was one of the first employees in Hemas' manufacturing operations and along with six other employees carried out manufacturing on a small scale at the Flower Road premises under the name Soraiya Industries, whose operations comprised eau de cologne and peppermint manufacture. When his employer, Sheik Hasannally passed away in 1980 he left Velu in the care of his oldest son Nuruddin with the promise that he would be looked after.

In 1977 during the commotions following the elections as well as during the riots of 1983, the Esufally family cared for Vellu. On both occasions he and his family found refuge at the Flower Road house. In 1983 in particular he was brought initially to the house and then sent for several months to the Nuwara Eliya estate.

Following the shift of manufacturing to Elakanda in 1985, Velu worked as a lift operator at the Hemas Drugs Building. To this day, Velu continues to work for the Esufally family, although presently under the Esufally Trust. He is presently senior building supervisor. In addition to the personal care he has received from the Esufally family, he acknowledges formal benefits of working for the company: staff loans, bonus, pay, as well as generally being looked after.

The company defines Velu's life. Although he has seen a lot of changes in the last 10 years, Vellu is confident that Abbas, Nuruddin's son will continue to look after him and his family after his father's death. Velu's four children have also been taken care of by the family. His elder son was sponsored by Soraiya Esufally; the technical studies of his second son in India by Nuruddin himself. The former works at Esufally Trust with him, the latter is employed at the Malaysia Airlines GSA, part of Hemas Travels. Vellu and his family know that the Esufally family appreciates their loyalty and hard work.

A3 – Key Company Milestones

DATE	COMPANY	FAMILY	POLITICAL CONTEXT
1948	Founding and Incorporation of Hemas (Drugs) Ltd. Carlo Earba agency	Break from EG Adamally & Co.	SL Independence
1951	Move to Hemas (Drugs) Building from Dam Street		
1962	Eau de Cologne franchise and factory		
1970-75	Entered tourism and other export/foreign exchange earner sectors • Seven Seas distribution • Garments- Cupid Industries Ltd. • Hemgems • Labour recruitment • Commodity exports • Serendib Hotels	Negative impact on income due to personal wealth tax and nationalization of family tea estates.	Restrictions on imports Foreign Exchange controls Land Reform Act Rent Control Act First JVP insurrection
1976	Hemtours launched		
1977	Management of Maldivian Hotels	Abbas enters business	Open Economy begins
1980	Travel Agency	Death of Sheik Hasannally Esufally	
1981		Husein joins business.	
1982	IATA[n] status for travel agency		
1983	Gave up management of Maldivian hotels	Mohsin retires Abid takes over Pharmaceuticals	Colombo riots Escalation of ethnic conflict.
1985	Eau de Cologne factory moves Ranbaxy agency	Imtiaz enters business	
1989			JVP terror campaign
1990	Marvel (first product innovation) launched		
1992	Apparel and Freight Forwarding businesses launched. Clogard launch and Unilever court battle	Murtaza enters business	
1993	Company reorganisation under Hemas Holdings (Pvt) Ltd. • Elimination of single balance sheet practice • Separation of management in each company • Dandex shampoo launched	Non-family members appointed as Directors	

DATE	COMPANY	FAMILY	POLITICAL CONTEXT
1994	GSA for Malaysia Airlines Kumarika launched		Regime change to PA
1996	GSA for Emirates Airlines Manufacturing facility for generic drugs Increased investment in Serendib Hotels, Peace Haven investment Prime Destinations (outbound agency) started		
1997-99	Closed down/sold most export businesses	Mohsin and Munnawar bought out	
1998	Entered into Procter and Gamble agency Hemas House (Cost of Rs. 166 mn)	Tea sales business with Munnawar's son Mohammed	
2001	Husein appointed CEO	Outside consultant to facilitate	LTTE attack on Katunayake airport
2002	Apparel sector reorganisation		Regime change to UNF
2003	GSA for LTU		
2003	Heladhanavi Power Project The IPO		
2004	Proctor & Gamble agency exit Velvet soap launched		Regime change to PA

A4 – List of Interviews

Board Members:

1. Husein Esufally
2. Imtiaz Esufally
3. Abbas Esufally
4. Murtaza Esufally
5. Serena Fonseka
6. Debu Bhatnagar
7. Simon Scarff
8. Lalith de Mel

Group Management Committee Members:

9. Stuart Chapman (Managing Director – Hemas Pharmaceuticals (Pte) Ltd. and Hemas Healthcare (Pte) Ltd.
10. Harshini Wickrema (Company Secretary and Head of Group Legal)
11. Irshad Halaldeen (Director – Group Human Resources)
12. Kishantha Nanayakkara (Managing Director – Hemas Power (Pte) Ltd.)
13. Malinga Arsakularatne (Business Strategist)
14. Neville Ruwanpathirana (Director - New Business Development)
15. Victor Abeysekera (Managing Director – Hemtours (Pte) Ltd.)

Others:

16. Shiromi Masakorala (Manager – Corporate Relations)
17. Dirk Grigson (Director - General Manager – Hemtours)
18. Sunil Dias (Director – Hemas Manufacturing)
19. Rochelle De Silva (Marketing Manager, Hemas Marketing)
20. R. Kulendran (40+ year employee, now Manager Projects and Transporation, Hemsons International (Pte) Ltd.)
21. Vellaran (Lift operator- 40+ year employee)
22. Lasantha Abeywickrama (Past executive and Director, now Director/ Senior Consultant, MTI Consulting)
23. Hilmy Cader (Past subsidiary Director and Consultant, now Chief Executive, MTI Consulting)

24. Mahanama Dodampegama (Past executive and Director, now Director, Baurs Pharmaceutical and Chemicals)

A5 – Interview Questionnaire

Study of Successful Sri Lankan Businesses.
Case Study 1/ Hemas Holdings Ltd.
Interview Questions- CEO Husein Esufally (up to first twenty questions)

General
1. What are the most important issues facing the business?

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2. What in your view are the core business/competencies of the group. Was this different to five years ago? Ten ? What were they then?

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3. What is the major focus of the company?

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4. What are the external problems that you worry about most?

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5. How has the company withstood international/local competition? Who do you worry about as competition, by industry/sector?

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6. What are the characteristics of the environment that the company operates in?

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7 Is the company able to innovate? For instance?

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8 What company do you benchmark? Why?
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9. What do other people see as the company's strengths?
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History
10. What do you feel are the ten most important milestones in the history of the company and why?
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11. Who else might give us a good view of the early years?
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12 Has the company demonstrated the ability to adapt and change? Give examples that best show this?
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13. Is there anything you would have done differently with hindsight or if you could have wished a different outcome to how the company stands today, what would that out come be?
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Family

14. What do you think are features that typically characterize a long time family business? Does Hemas have these characteristics-? Where does it differ from the stereotype?
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15. What changes from a family structure have you put in place to help the company move forward?
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16. What was the early demarcation of sectors among family members? Which were the successes? Failures?
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17. How has the board evolved over the years?
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18. How much time do you spend on strategy formulation? What are the structured ways in which planning is done within the group? What are the external props you use to facilitate strategy or is it all organic?.
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19. What are the key initiatives in your memory that led to competitive advantage? What in your mind is your competitive advantage? Has it changed recently/ over the years?

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20. Let's talk about company values and how they are enshrined in culture if it is. Has it changed as the market and the world changed or are they a constant?………………………………………………………………………………
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Specific- functional heads to answer

Marketing

21. What is the Brand equity of Hemas as a company?

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22 What is the market share of the company in its various product lines?

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23 What are the strongest brands?

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24. How important is marketing / advertising in the company ethos?

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25 What are the least profitable product lines for the company?

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26. What products or services do competitors offer that Hemas doesn't?

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27. Is the product line lacking in any market segment? How do you drive NPD?

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HR

27 . Does the company have a strong team of skilled employees – how do you find high flyers or do you create them?

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28 How is the morale of employees? What are your feedback mechanisms to track employee satisfaction?

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29. Are there rewards in place to create an atmosphere conducive to excellence?

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30 Are there employees with skills unique in the industry?
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31 What are the PDR processes in place (performance review systems).
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32 How strong are the communication skills of team members and team leaders?
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33 Describe the impact of the company's stock option program
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34. What is the company's emphasis on professional development?
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34. How are values instilled in the company?
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Finance

35. What are the major sources of revenue and profit?
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36. Is the cost of capital an advantage or barrier to growth relative to industry and competition?
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37 Stock prices – do you think it represents true value?
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38.What has been your main source of funding? Also talk about the IPO and how you walked down that path.
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39. With which banks have you been sustaining strong banking relationships?
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35. Describe your budgeting, cash, receivable management processes.
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36. What is/ has been the company's dividend policy Taxes, tax planning
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37.What is the company's investment strategy?
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Operations

38. Does the company harness information technology effectively? How? Describe the processes in place.
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39 .How does the company manage its supply chain (including inventories, logistics, sourcing, supplier evaluation, transportation, storage)?
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40. What is the policy on real estate management including appraisal and disposal?

Media

41 What is the company's PR strategy? What is the perception you wish to create?
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42 How is company communication maintained within the group?
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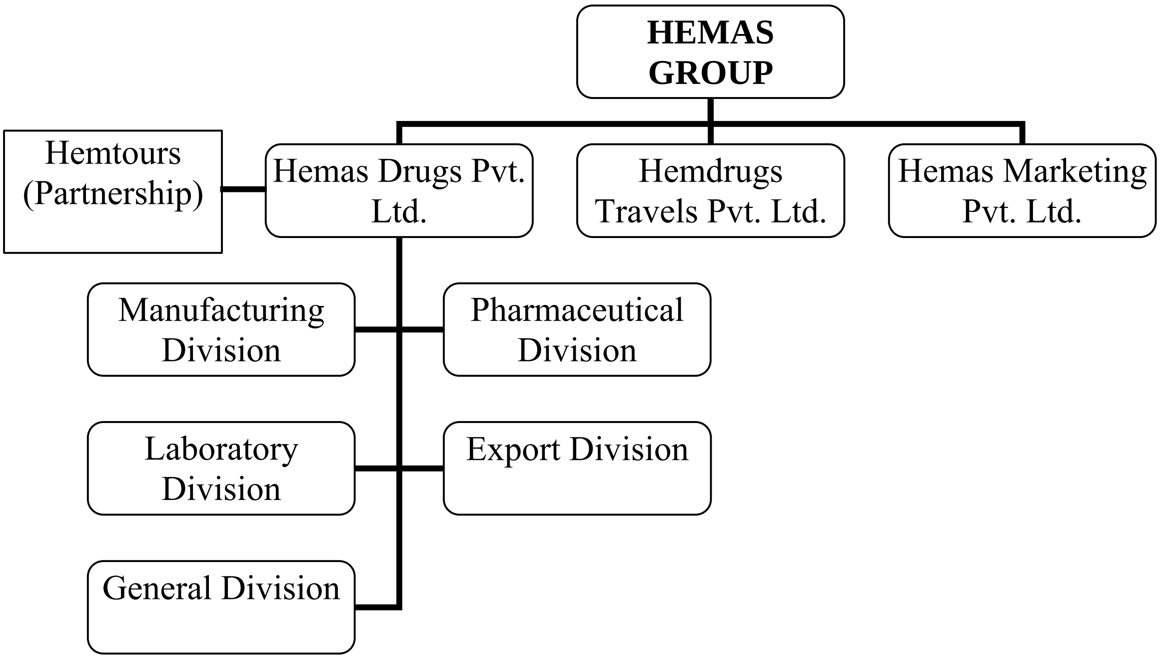
A6 – Pre-1993 Corporate Structure



A7 - Hemas Statistics

	1960s*	1970s*	1980s*	1990s	2000s
Annual Sales (Rs)	N/A	N/A	150 mn	1574 mn	8797 mn
By Sector (Rs.):					
Personal Care	N/A	N/A	100 mn	900 mn	2897 mn
Pharmaceuticals	N/A	3 mn	12 mn	479 mn	2411 mn
Leisure	N/A	N/A	N/A	86 mn	445 mn
Transport	N/A	N/A	N/A	51 mn	352 mn
Strategic Investments	-	-	-	-	2957 mn
Profit (Rs.)	N/A	N/A	5mn	96 mn	803 mn
Assets	N/A	N/A	100mn	1413 mn	9651 mn
Employees					
No.	N/A	N/A	200	1000	1150
No. of senior managers					
Ownership structure (%)	Privately Held				Listed
Sheikh Hasannally Esufally	-	2	-	-	-
Sons (each)	-	24.5	24.5	-	-
Grandsons	-	0	2	100	75
Outsiders	-	-	-	-	25
Salesforce					
Pharma	N/A	N/A	4	50	150
Personal Care	N/A	N/A	15	40	150
Distributorships					
Pharma	-	-	0	10	30
Personal Care	-	-	-	10	120
Penetration (No. of stores and %)					
Pharma	N/A	N/A	1000	1200	2000 (96%)
Personal Care	N/A	N/A	N/A	5000	65000
Agencies					
Pharma	2	3	5	8	30
Personal Care	-	-	3	5	5
GSA's	-	-	-	2	8
Subsidiaries				9	23
Brands	N/A	N/A	3	14	40

Notes:
1. All figures before 1990 are approximate and are from Corporate memory instead of corporate financial statements.
2. The numbers in the above table are intended to provide a sense of the magnitude of growth of the company over the past 25 years.
3. N/A = Not Available