

## Falcon Energy Group

13 Aug 09

### Results Review

#### Still Ready For The East Wind

**Results:** On 7<sup>th</sup> Aug 2009, Falcon announced a flat half year result of US\$28m revenue and US\$12m profit, comparable to its 9 month 2008 result of US\$44 m revenue and US\$20m profit. 1H09 was rather unexciting for Falcon as the market demand was weak and demand only started to pick up during 2Q09. Nonetheless, the company managed to put up a reasonable performance.

**Reason for 1H performance:** A chat with the management reveals that **some of the vessel was chartered for most of the 1H09**. The rest of the ships were under modification earlier in the year in preparation for their next chartering.

**What can we expect for 2H09?:** One of the vessels underwent a long term modification and was recently sent to the Middle East. This vessel is chartered at a fee more than twice of Falcon's average vessel rate a day with an initial mobilization fee. With a significant chartering contract time, this ship alone is going to generate high revenue with a lucrative margin for Falcon in 2H09. On top of that, 2 other vessels will also be deployed in 2H09.

**Is our forecast off?:** We estimate a revenue of US\$77m for FY09 with a profit of US\$33m. This means that the company has to attain revenue of US\$49m for 2H09 and a profit of US\$21m. With most of the vessels chartered and more contribution from Longzhu Group of Companies, we believe that Falcon is more than capable of meeting our expectation for FY09.

**Everything is still in place:** Falcon is currently in talks to purchase new vessels as the value has dropped substantially due to speculative supply (Ready for the East Wind, 05/08/2009). Several projects with some of Longzhu Group's clients are still under negotiation and Falcon is expected to clinch at least one substantial deal in 2H09.

### Increase Exposure

Target Price **S\$1.01**  
 Prev Closing Price **S\$0.80**

#### Main Activities

Falcon is an investment holding company which offers a spectrum of services from exploration and drilling phase to the post production stage. The business is divided into three segments: Marine, Oilfield Service and Oilfield Project.

#### Financial Highlights

(Y/E Dec )US\$m	FY08-15 mths	FY09F	FY10F
Revenue	73.8	76.8	99.8
Gross Profit	41.6	42.5	55.0
Net Profit	36.1	32.8	40.7
EPS (US cts)	5.15	4.44	5.50

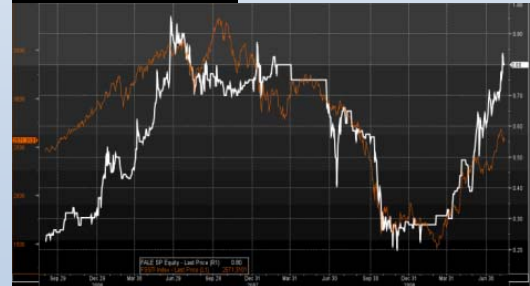
Source: Company, SIAS Research

#### Key ratios (FY09F)

PER	12.6
P/BV	3.9
ROA	15.9%
ROE	21.9%
Net Debt to Equity	Net Cash
Current ratio	2.36

Source: SIAS Research

#### Indexed Price Chart



Source: Bloomberg

52wks High-Low **S\$0.835/S\$0.205**  
 Number of Shares **739 m**  
 Market Capitalization **S\$591.2m**

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**Valuation:** We maintain our **Increase Exposure** call on Falcon based on the Economic Profit valuation of S\$1.01. The higher charter rate as well as contribution from Longzhu Group will boost Falcon's 2H09 to our expectation. The 'sweet spot' remains for the firm to leverage on.

**Figure 1: Economic Profit Valuation**

USD'000	2008-15 mths	2009F	2010F	2011F	2012F	2013F
Revenue growth	91.4%	30.0%	30.0%	28.0%	26.0%	3.0%
COGS (% of Revenue)	-43.7%	-44.7%	-44.9%	-45.0%	-45.5%	-46.0%
Admin Cost (% of Revenue)	-13.8%	-13.5%	-14.0%	-14.1%	-14.1%	-14.4%
EBIT	37,918	35,447	44,565	56,006	68,998	69,788
Tax on EBIT	(670)	(886)	(1,337)	(2,240)	(3,450)	(4,885)
Deferred Tax Liability	(62)	(84)	(126)	(210)	(321)	(449)
NOPLAT	37,186	34,477	43,102	53,556	65,227	64,454
Beg Book Value	109,767	189,141	223,942	286,237	366,072	462,002
WACC		0.0932	0.0932	0.0932	0.0932	0.0932
Capital Charge		17,628	20,871	26,677	34,118	43,059
Economic Profit		16,849	22,231	26,879	31,109	21,396
Terminal						348,694
Discount Rate		0.97	0.89	0.81	0.74	0.68
Present Value		16,356	19,740	21,833	23,115	14,542
Starting Book Value		189,141				
Explicit Value		95,586				
Terminal Value		236,999				
Value of Firm		521,726				
Number of Shares		739,000				
Value per Share		US\$0.71				
US Dollar Conversion		1.43				
Value in S\$		\$1.01				

Source: SIAS Research Estimate

## Results Review

Figure 2: Financial Forecast and Estimate

Profit and Loss	2007	2008-15 mths	2009F	2010F	2011F	2012F	2013F
Revenue	38,582	73,838	76,792	99,829	127,781	161,004	165,834
Cost of Sales	(17,738)	(32,283)	(34,326)	(44,823)	(57,501)	(73,257)	(76,284)
Gross Profit	20,844	41,555	42,466	55,006	70,280	87,747	89,551
Other operating income	2,615	6,236	3,000	3,100	3,200	3,300	3,400
Administrative Cost	(4,344)	(10,163)	(10,367)	(13,976)	(18,017)	(22,702)	(23,880)
Finance Cost	(660)	(1,159)	(1,793)	(2,641)	(3,619)	(4,759)	(5,676)
Share of profit of associate	-	290	348	435	544	653	718
Profit before tax	18,455	36,759	33,654	41,924	52,387	64,239	64,112
Income tax	(253)	(650)	(841)	(1,258)	(2,095)	(3,212)	(4,488)
Profit from continuing operations	18,202	36,109	32,813	40,666	50,291	61,027	59,624
Loss from discontinued operation	(830)	-	-	-	-	-	-
Profit and Loss for Year	17,372	36,109	32,813	40,666	50,291	61,027	59,624

Cash flow	2007	2008-15 mths	2009F	2010F	2011F	2012F	2013F
Profit before income tax	17,625	36,759	33,654	41,924	52,387	64,239	64,112
Change in operating cashflow exclude working capital	3,854	5,883	8,447	9,714	12,367	15,903	17,552
Operating cash flows before movements in working capital	21,479	42,642	42,101	51,637	64,754	80,142	81,663
Change in working capital	(13,971)	10,247	(6,551)	(1,684)	(3,256)	(3,911)	(1,434)
Cash generated from operations	7,508	52,889	35,550	49,953	61,498	76,231	80,229
Income tax paid	(6)	(588)	(757)	(1,132)	(1,886)	(2,891)	(4,039)
Net cash from operating activities	7,502	52,301	34,793	48,821	59,613	73,341	76,190
Net cash used in investing activities	(34,213)	(52,707)	(15,767)	(45,413)	(54,676)	(65,617)	(19,665)
Net cash from financing activities	26,045	7,240	18,303	9,245	11,782	14,643	1,835
Net change in cash and cash equivalents	(666)	6,834	37,329	12,654	16,719	22,366	58,360
Effect of exchange rate changes	2	11	(20)	(25)	(30)	(33)	(35)
Cash and cash equivalents at beginning of year	3,182	2,518	9,363	46,672	59,301	75,990	98,323
Cash and cash equivalents at end of year	2,518	9,363	46,672	59,301	75,990	98,323	156,648

Balance Sheet	2007	2008-15 mths	2009F	2010F	2011F	2012F	2013F
<b>Current Assets</b>							
Cash and cash equivalents	2,518	10,271	45,764	60,301	75,990	97,323	156,648
Trade receivables	11,663	12,936	12,804	15,013	19,347	24,547	27,781
Other receivables	6,149	6,981	6,778	7,948	10,242	12,995	14,708
Inventories	2,715	1,188	2,033	2,384	3,187	4,043	4,576
Total	23,045	31,376	67,379	85,646	108,766	138,908	203,712
<b>Non Current Assets</b>							
Other receivables	4,800	1,526	3,239	3,886	5,007	6,353	7,190
Property, plant and equipment	67,833	119,857	128,392	166,066	210,980	264,386	270,945
Investment in associate	-	5,790	7,123	6,731	8,362	9,107	8,924
<b>Current Liabilities</b>							
Trade payables	4,586	5,901	5,395	6,371	8,288	10,722	12,412
Other payables	6,108	17,144	13,322	15,038	18,418	22,229	25,422
Finance leases	28	16	13	10	7	4	1
Borrowings	3,113	7,215	9,380	12,662	16,208	19,936	21,730
Income tax payable	254	316	400	526	735	1,057	1,505
Total	14,089	30,592	28,510	34,608	43,657	53,947	61,070
<b>Non Current Liabilities</b>							
Finance leases	46	43	31	24	17	10	3
Borrowings	9,019	21,129	27,468	37,081	48,947	63,632	69,359
Total	9,065	21,172	27,499	37,105	48,964	63,642	69,362
Share capital	8,132	179,524	190,224	190,224	190,224	190,224	190,224
Capital reserve	165,892	-	-	-	-	-	-
Merger reserve	(148,064)	(154,954)	(154,954)	(154,954)	(154,954)	(154,954)	(154,954)
Revaluation reserve	3,262	3,262	3,262	3,262	3,262	3,262	3,262
Foreign currency translation reserve	2	(456)	(630)	(804)	(1,218)	(1,573)	(2,022)
Accumulated Profits	43,300	79,409	112,222	152,888	203,179	264,206	323,830
Total Equity	72,524	106,785	150,124	190,615	240,493	301,166	360,340

Source: SIAS Research Estimate

**Definition:**

**Increase Exposure** – The current price of the stock is significantly lower than the underlying fundamental value of the firm. Readers can consider increasing their exposure in their portfolio to a higher level.

**Invest** – The current price of the stock is sufficiently lower than the underlying fundamental value of the firm. Readers can consider adding this stock to their portfolio.

**Fairly Valued** – The current price of the stock is reflective of the underlying fundamental value of the firm. Readers may not need to take actions at current price.

**Take Profit** – The current price of the stock is sufficiently higher than the underlying fundamental value of the firm. Readers can consider rebalancing their portfolio to take advantage of the profits.

**Reduce Exposure** - The current price of the stock is significantly higher than the underlying fundamental value of the firm. Readers can consider reducing their holdings in their portfolio.

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