

Falcon Energy Group

Healthy Recovery in Marine Division

Falcon Energy Group (Falcon) posted its strongest quarterly Marine performance over the last 12 quarters, with the division's revenue and gross profit rising US\$4.42m and US\$8.94m YoY to US\$16.03m and US\$8.94m respectively.

Demand for support vessels, particularly work barges, has been relatively strong recently and chartering rates are up about 10% YoY. We expect this phenomenon to support Falcon's FY14 numbers. However, 5Q FY13 (Falcon recently adjusted its financial year end to March 2013) is expected to be weak due to the monsoon season in Malaysia, which led to the return of some vessels.

Falcon has also signed a preliminary agreement with PetroVietnam Drilling & Well Service Corporation to set up a JV to provide drilling and related services. We expect Falcon to sell one of their rigs to this JV and the other one to other interested parties. We remain optimistic about the company's FY14 numbers and recommend **Increase Exposure**.

Key Developments:

Results Summary: 4Q revenue dipped 4.3% YoY to US\$24.4m mainly due to lower contribution from oilfield services and oilfield projects. Management is now focusing more on the marine and drilling services divisions on the back of the current active O&G market. Gross profit rose US\$6.03m YoY to US\$12.12m with the marine division contributing the bulk of the gains. Administrative expenses decreased US\$6.85m due to the absence of a one-off allowance of trade doubtful debts in 4Q FY11. Share of profit from associates was -US\$1.4m due to goodwill written-off for vessel sold in 2012 against profit from CH Offshore. Consequently, Falcon recorded US\$5.2m for 4Q 2012.

Borrowings rose about US\$23.1m as the company ordered a few vessels and commenced the construction of two JV rigs. Business fundamentals remain strong as cashflow before working capital was US\$24.5m

Increase Exposure

- Intrinsic Value S\$0.480
- Prev Close S\$0.365

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 Services and Oilfield Projects. The Resource divisions and Drilling Services division were established recently.

Financial Highlights

(Y/E Dec) US\$m	FY10	FY11	FY12F
Revenue	64.6	79.9	114
Gross Profit	24.6	17.9	35.9
PATMI	11.3	3.3	13.6
EPS (US cts)	1.39	0.40	1.39*

*: Include Warrants
Source: SIAS Research Estimates

Key ratios (FY14F)

PER*	17.5
P/BV*	1.3
ROE	7.9%
Debt/Equity	71.9%
Current ratio	1.32

*: Include Warrants
Source: SIAS Research Estimates

Indexed Price Chart

Green (FSSTI)
White (Falcon)



Source: Bloomberg

52wks High-Low 41.5 cents/19.6 cents
Number of Shares 814.1 m
Market Capitalization S\$297m

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Figure 1: Falcon's Segment Breakdown

Revenue (US\$m)	1Q 2011	2Q 2011	3Q 2011	4Q 2011	1Q 2012	2Q 2012	3Q 2012	4Q 2012
Marine	2.88	1.80	6.69	11.61	8.58	9.55	10.42	16.03
Oilfield Services	10.19	7.58	15.30	10.50	23.98	3.56	5.40	6.33
Oilfield Projects	3.31	3.34	3.38	3.37	3.34	3.34	2.01	2.02
Gross Profit (US\$m)								
Marine	-1.32*	-2.19*	2.25	0.66	2.09	1.85	3.06	9.60
Oilfield Services	2.51*	2.27	2.59	3.56	2.04	1.15	1.04	1.87
Oilfield Projects	1.84	1.94*	1.88	1.87	1.95	1.95	0.63	0.64

*: SIAS Research Estimates

Source: SIAS Research

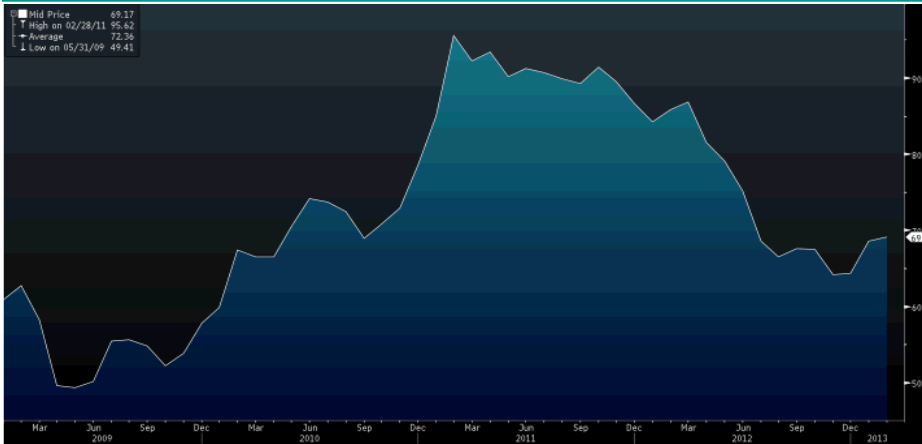
Company Update: Falcon recently entered into a preliminary agreement with PetroVietnam Drilling & Well Service Corporation to set up a JV company to provide drilling and related services. We reckon that Falcon may sell one of their rigs to this JV and stay as a dormant investee in the JV. As for the other rig, there are a few interested parties and Falcon's 45% stake in the two rigs may reap a one-off profit of about US\$18m. Falcon's initial share of down payment for the rigs was merely US\$16m. After the plans for these two rigs are finalized, Falcon has the option of ordering two more rigs at a preferred rate.

The marine division had a spectacular 4Q with utilization rate of about 80%. 5Q FY13 is likely to be weak but we expect the trend to pick up thereafter. We project utilization rate for FY14 to be around 70%. We will also see the delivery of 2 MPSV in June/July 2013 and some of the existing vessels may have the opportunities to go under longer term charters. We remain optimistic about the marine division's outlook.

On the resource division, there were cases of illegal mine raids in Indonesia and that led to a slight recovery in coal prices to the high US\$60+/ton level. However, Falcon will probably initiate production only if coal prices recover to above US\$80/ton level. For the time being, the company is still exploring for new concessions in the region.

Forecasts and Outlook: We have taken into consideration the better chartering market condition, contribution from the new vessels and some level of coal trading activities into our model. We also included our FY15F numbers and did not expect any share of profit from the drilling services division. Maintain **Increase Exposure** with an upgraded intrinsic value of S\$0.480.

Figure 2: Indonesia Coal Price (US\$/ton, for 5400kcal)



Source: Bloomberg

Figure 3: Economic Profit Model

US\$ '000	2011	5Q 2012F	2014F	2015F
EBIT	10982	21281	25224	32007
Tax on EBIT	-2369	-745	-2522	-3201
Deferred Tax Liability	-1060	721	0	0
Minority Interest	-2282	-212	-500	-500
NOPLAT	5271	21045	22202	28306
Total Invested Capital	282459	305967	294221	284168
WACC	7.6%	9.1%	7.4%	7.4%
Capital Charge	21384	27745	21695	20954
Economic Profit		-6700	507	7352
Terminal				165254
Discount Rate		0.98	0.91	0.85
Present Value		-6566	462	6250
Book Value	189030			
Explicit Value	-6104		Risk Free	2.5%
Terminal Value	140469		MRP	7.0%
Value of Firm	323395		Cost of Equity	9.50%
Number of Shares	976920		Cost of Debt	5.0%
Input from Warrant	52096		Terminal G	2.8%
Value per Share (US\$)	0.384		WACC	8.7%
US Dollar Conversion	1.25			
Value in S\$	0.480			

Source: SIAS Research Estimates

Figure 4: Financial Forecasts and Estimates

US\$ '000	2010	2011	5Q 2012F	2014F	2015F
Revenue	64610	79949	114224	116508	142140
Gross Profit	24615	17858	35879	40778	52592
Net Income Before Taxes	12151	7084	14281	18262	25144
Net Income After Taxes	11684	5556	13781	16436	22630
Total Current Assets	49872	76558	95268	101370	105400
Total Non-Current Assets	248460	291758	309101	325456	338455
Total Current Liabilities	33337	67909	71391	77027	71427
Total Non-Current Liabilities	69719	102969	124712	125097	125096
Total Equity	195276	197438	208266	224702	247332
Net Income Before Tax	12151	7084	14281	18262	25144
Cash from Operating Activities	15692	-16087	1661	31744	18399
Cash from Investing Activities	-117967	-14134	-25635	-23355	-11100
Cash from Financing Activities	67378	31080	24867	602	-5000
Net Change in Cash	-34897	859	893	8991	2299
Net Cash - Beginning Balance	47054	12303	13097	14305	23296
Net Cash - Ending Balance	12303	13097	14305	23296	25595
Inventory Days	6	58	105	131	108
Receivable Days	204	164	120	112	90
Payable Days	91	93	105	113	105
ROE	6.4%	2.9%	7.1%	7.9%	10.0%
ROA	4.5%	1.7%	3.6%	4.0%	5.2%
Debt/Equity	50.1%	69.4%	77.4%	71.9%	63.1%
Current Ratio	1.50	1.13	1.33	1.32	1.48
P/E*	20.6	71.1	20.6	17.5	12.6
P/B*	1.2	1.2	1.4	1.3	1.2

*: Include Warrants for FY12F and FY13F
 Source: SIAS Research Estimates

Rating Definition:

Increase Exposure – The current price of the stock is significantly lower than the underlying fundamental value. 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.

IMPORTANT DISCLOSURE:

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