

Falcon Energy Group

Expansion Plans for Marine and Resource Divisions

Falcon Energy Group (Falcon) recorded an exceptional FY14 numbers with revenue and PAT of US\$351m and US\$102m vs our estimates of US\$294m and US\$87m respectively. The stronger set of results was partially boosted by 1) exceptional performance from the oilfield services division, 2) US\$7.3m disposal gain from the 50% sale of one of its multi-functional support vessels to a Mexican party and 3) the US\$12.8m share of allowance of doubtful trade debts from CH Offshore was shifted to FY12, causing the share of profit of associates to soar to US\$7.2m in FY14. The adjustment of the latter was made under the advice of the external auditors so as to align the timing of the provision with that of CH Offshore.

The company is poised for several growth plans, including increasing the number of vessels in the marine division, commencing operations at the coal mines and the potential sale or leasing of its rigs. We expect these developments to propel revenue and profit in FY15 and FY16. Maintain **Increase Exposure** with an intrinsic value of S\$0.565.

Results Summary: The marine division continued to perform with revenue of US\$17.1m and gross profit of US\$4.3m. The figures were slightly lower QoQ as some of the vessels were sent for maintenance and modification – we expect the numbers of the next two quarters to be better.

The oilfield services surprised us with revenue and gross profit of US\$76m and US\$9m respectively. The division was engaged in in the purchase of some big ticket items for a shipyard and we may expect some more work (albeit lower value) in the next few quarters. The oilfield projects division continued to operate as per normal and there was no contribution from the drilling division.

Other receivables grew US\$67m QoQ to US\$123m probably due to the big ticket items from the oilfield services division. Correspondingly, other payables jumped US\$75m QoQ to US\$107m. Cash from operating activities stood at US\$127m for FY14. Falcon also declared 1 S cent final dividend, leading to a full year dividend payout of 1.5 S cent.

Increase Exposure

- Intrinsic Value S\$0.565
- Prev Closing Price S\$0.385

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 Mar)US\$m	FY12*	FY14	FY15F
Revenue	116	351	166
Gross Profit	33.0	117	60.0
PAT	10.4	102	33.2
EPS (US cts)	1.2	7.5	4.0

*: 5 quarters

Source: Voyage Research Estimates

Key ratios (FY15F)

PER	7.7
P/BV	0.9
ROE	13.0%
Debt/Equity	69%
Current ratio	1.6

Source: Voyage Research Estimates

Indexed Price Chart

Green (FSSTI)
Black (Falcon)



Source: Bloomberg

52wks High-Low 45.5 cents/31.5 cents

Number of Shares* 818m

Market Capitalization S\$315m

*: Ex warrants

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Figure 1: Segment Numbers

Revenue (US\$m, CY)	4Q 2011	1Q 2012	2Q 2012	3Q 2012	4Q 2012	5Q 2012	1Q 2014	2Q 2014	3Q 2014	4Q 2014
Marine	11.61	8.58	9.55	10.42	16.03	8.75	16.98	17.84	18.62	17.10
Oilfield Services	10.50	23.98	3.56	5.40	6.33	6.84	7.19	35.84	24.14	75.87
Oilfield Projects	3.37	3.34	3.34	2.01	2.02	6.04	2.00	2.02	2.02	2.73
Drilling								127.80	0.01	0.00
Gross Profit (US\$m)										
Marine	0.66	2.09	1.85	3.06	9.60	-1.41	7.03	5.51	5.88	4.33
Oilfield Services	3.56	2.04	1.15	1.04	1.87	1.98	1.62	4.06	5.44	9.05
Oilfield Projects	1.87	1.95	1.95	0.63	0.64	4.60	0.64	0.58	0.68	0.68
Drilling								71.44	0.01	

Source: Voyage Research

Operations Update: Falcon has approximately half of its vessels operating in Indonesian waters and some of its vessels are operating in Malaysia and Brunei. These activities helped to lift its vessel utilization rate and we speculate that the company may plan to get more vessels given that most of their vessels are chartered out. The approximate number of new vessels may vary from four to ten. We also understand that Falcon is also performing agency work for some of the Indonesian operators and charterers. Falcon may have future plans for their Indonesia-flagged vessels and operations.

The plan to embark on coal mining is in progress and Falcon will engage a third party contractor to operate the mines – they are currently reviewing quotations from third party contractors. The company plans to kick start the project over the next six months. For the drilling division, the company continues to receive numerous enquiries to charter or acquire the rigs. We reckon that the consortium may seek to sell two of the rigs and charter out the remaining three. We may get more updates towards the end of 2014 or early 2015.

Forecast and Summary: Falcon's 4Q numbers were mainly boosted by the oilfield services division and other one-off gains. We expect the operating profit to improve further in FY15 given that 1) marine division is expected to have a larger operating fleet with higher utilization rate, 2) contribution from the resource division may kick in and 3) oilfield services division is likely to have continuous work in FY15. For conservative reasons, we did not include any potential gain from the sale of rigs into our model. We also introduced our FY15 numbers and expect continuous growth in revenue and PAT, mainly due to greater contribution from the marine, resource and coal mining divisions. Our model points to an improved intrinsic value of S\$0.565.

Figure 2: Economic Profit Valuation

US\$ '000	2011	5Q 2012	2014	2015F	2016F
EBIT	10982	17512	113454	43895	47317
Tax on EBIT	-2369	-1097	-6415	-3073	-3312
Deferred Tax Liability	-1060	405	-357	0	0
Minority Interest	-2282	-591	-41353	-500	-500
NOPLAT	5271	16229	65329	40323	43505
Total Invested Capital	282459	-117279	-126577	385961	453246
WACC	15.6%	-20.5%	7.9%	7.9%	7.9%
Capital Charge	44042	24066	-9969	30397	35697
Economic Profit			75298	9925	7808
Terminal				209666	99143
Discount Rate				0.93	0.86
Present Value				9201	6710
Book Value	224303				
Explicit Value	15910		Risk Free	2.5%	
Terminal Value	141742		MRP	7.5%	
Value of Firm	381956		Cost of Equity	10.00%	
Proceed from warrant	28208		Cost of Debt	5.0%	
Number of Shares	905400		Terminal G	3.0%	
Value per Share (US\$)	0.453				
US Dollar Conversion	1.25				
Value in S\$	0.566	~0.565			

Source: Voyage Research

Figure 3: Financial Forecasts and Estimates

US\$ '000	2011	5Q 2012	2014	2015F	2016F
Revenue	79949	116195	350788	166168	174169
Gross Profit	17858	33005	117015	59820	64443
Net Income Before Taxes	7084	11075	108241	35737	38902
Net Income After Taxes	5556	10381	102121	33236	36179
Total Current Assets	76558	92853	216968	136869	139836
Total Non-Current Assets	291758	295252	358232	375862	400861
Total Current Liabilities	67909	74743	177432	87089	91089
Total Non-Current Liabilities	102969	118057	138541	138065	138065
Total Equity	197438	195305	259227	287577	311543
Net Income Before Tax	7084	11075	108241	35737	38902
Cash from Operating Activities	-16087	16050	126684	13931	29277
Cash from Investing Activities	-14134	-30998	-74513	-13730	-21100
Cash from Financing Activities	31080	14522	-24458	2534	-8213
Net Change in Cash	859	-426	27713	2734	-36
Net Cash - Beginning Balance	12303	13097	12896	40600	43334
Net Cash - Ending Balance	13097	12896	40600	43334	43298
Inventory Days	58	39	1	4	4
Receivable Days	164	179	127	279	182
Payable Days	93	113	115	256	85
ROE	2.9%	5.5%	47.7%	13.0%	0.0%
ROA	1.7%	2.7%	21.2%	6.1%	0.0%
Debt/Equity	69.4%	79.0%	73.5%	68.6%	64.5%
Current Ratio	1.13	1.24	1.22	1.57	1.54
P/E	76.6	25.6	4.1	7.7	7.0
P/B	1.3	1.3	1.0	0.9	0.9

Source: Voyage 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.

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