

Favelle Favco (FFB MK)

Cash dynamo

Initiate with BUY

Favelle Favco (Favelle) is a cash dynamo and financially resilient in a capex-heavy, cyclical-driven O&G industry. Its cranes manufacturing and automation businesses are asset-light and cash-generative. Favelle is net cash and has consistently paid dividends, atypical for this industry. Favelle offers earnings growth (3-year NP CAGR of 13%), high dividend yields (5-6%) and undemanding valuations (7x PER) vs. peers. Accretive M&A, akin to the acquisition of Exact in 2018, would add to upside.

An asset-light growth stock in a rising orders market

Prospects are bright for Favelle to capitalise on the global O&G offshore investment upcycle via its cranes construction/ maintenance/ rental and automation businesses. 80% of its cranes manufacturing revenue are O&G related. Orderbook visibility is improving; up 32% YoY end-Nov 2019 (to RM564m) after having bottomed in 2018. We expect Favelle to grow its order backlog to MYR600m-800m in FY19E-21E, a realistic target (2014 peak: MYR1.1b) that underpins 3-year 13% net profit CAGR (FY18-FY21).

Cash generative, dividend yielding

A remarkable feature of Favelle is that it has always been running on a profit, even during the downcycle (2014-17), which is a testament to its cost-focused and bottom line-driven management. It has been net cash since 2010 and has consistently generated positive FCF. We estimate FCF of MYR39m-MYR84m in FY19-21, equivalent to FCF yields of 6%-14%, a strong foundation for consistent dividend payouts. At a 40% DPR, this translates into an attractive dividend yield of 5-6%.

Target price of MYR3.65

Our TP is based on 0.6x EV/order backlog of MYR725m, pegged to 1SD above its 5-year mean valuation. The orders are premised on its average revenue for FY20-21. We prefer this valuation method over others for it captures the cyclical nature of its orderbook and takes into account its balance sheet and cashflows aspects. Our TP, which implies 9.7x PER and 4.1% dividend yield for FY20 is undemanding vis-à-vis its peers.

FYE Dec (MYR m)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue	526	531	620	691	758
EBITDA	106	106	127	139	152
Core net profit	75	65	75	84	93
Core EPS (sen)	33.7	29.5	33.9	37.6	42.0
Core EPS growth (%)	(20.4)	(12.5)	14.9	11.1	11.6
Net DPS (sen)	13.5	13.5	13.5	15.0	16.8
Core P/E (x)	8.1	7.8	8.3	7.4	6.7
P/BV (x)	1.0	0.8	0.9	0.8	0.8
Net dividend yield (%)	4.9	5.9	4.8	5.4	6.0
ROAE (%)	10.3	9.8	11.0	11.4	11.8
ROAA (%)	6.3	5.2	5.6	5.9	6.2
EV/EBITDA (x)	2.5	2.5	2.9	2.4	1.9
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	na	na	na
MKE vs. Consensus (%)	-	-	na	na	na

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BUY

Share Price MYR 2.80
12m Price Target MYR 3.65 (+30%)

Company Description

Favelle Favco provides cranes manufacturing & maintenance services

Statistics

52w high/low (MYR)	3.02/2.23
3m avg turnover (USDm)	0.1
Free float (%)	24.2
Issued shares (m)	223
Market capitalisation	MYR624.7M USD149M

Major shareholders:

Muhibbah Engineering (M) Bhd.	58.8%
MAC NGAN BOON	4.3%
Yayasan Hasanah	2.2%

Price Performance



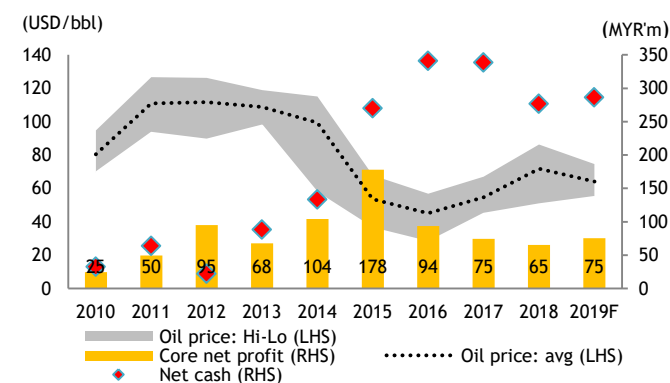
	-1M	-3M	-12M
Absolute (%)	4	2	21
Relative to index (%)	6	5	30

Source: FactSet

Value Proposition

- Predominantly a crane manufacturer (offshore, tower, wharf & crawler) with 7 operating facilities worldwide. It also offers rental, service & maintenance works of cranes.
- Also involved in the provision of design, engineering & maintenance services for the O&G industry via its 70%-owned Exact Group, acquired in Jul 2018 for MYR91m.
- Entrenched to capitalise on the order replenishment upcycle as O&G activities pick up.

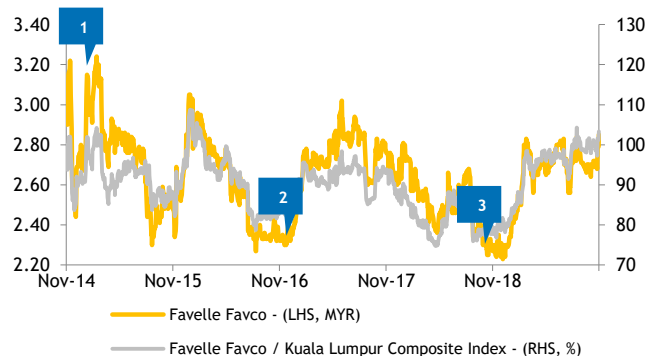
Oil price relative to cash level & profitability



Source: Company, Maybank Kim Eng

Price Drivers

Historical share price trend



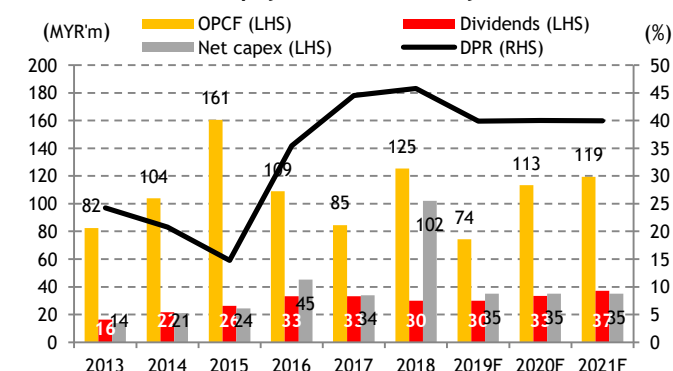
Source: Company, FactSet, Maybank Kim Eng

- The beginning of the fall in crude oil price to sub-USD100/bbl.
- Recovery in the crude oil price post OPEC's agreement to cut oil production to 32.5m bpd.
- Acquired a 70% stake in Exact Group for MYR91m in Jul 2018.

Financial Metrics

- Order backlog, margins, order replenishment and opex are Favelle's key earnings drivers. Variation in any of these parameters will impact profitability.
- Current order backlog was MYR564m as at Nov 2019 and is on the rise.
- Has a cost conscious mind set. A profitable company even during the downcycle, with a focused management team.
- Financially resilient. Net cash, consistently generating positive FCF & paying dividends; this is atypical in the O&G sector.

Consistent dividend payouts from healthy cashflows



Source: Company

Swing Factors

Upside

- Rebound in crude oil price will be a share price driver.
- Recovery in order replenishment and margin expansion are key catalysts.
- Special/ higher dividend payment serves as a potential positive.
- An enhancing M&A exercise would likely generate excitement.

D downside

- Further weakness in oil price will hurt share price performance.
- Execution mishap, cost overruns and/ or absence of new orders will cause adverse reaction.
- Acquisition of non-core assets or ill-usage of capex will not be well received.

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Investment thesis

Entrenched to capitalise on the O&G upcycle

Global sanctioning for O&G activities is rapidly increasing. Greenfield project commitments, especially offshore investments, have clearly picked up, with high volume of potential works available over the next few years. Based on a bottom-up mapping of the future line-up of projects, about USD369b worth of offshore E&P investment are expected over 2019-21E vs. USD155b in the previous 3 years; (2016-18), with the majority of the focus in Asia, Africa and Latin America.

Favelle Favco (Favelle)'s operations, namely its cranes manufacturing and intelligent automation businesses, are well positioned to ride on the O&G upcycle. We are seeing a progressive recovery in its order backlog (bottomed in 2Q18) on the back of a rise in the tender pipeline.

Has one of the finest financials in the O&G market

Unlike most of its peers in the services space, Favelle has always been running at a profit, even during the 2014-17 downcycle, a testament to its operating resilience and cost-driven and bottomline-focused management. Favelle has been in a net cash position since 2010 and consistently generates positive free cash flows (FCF). We estimate its net cash/share to grow to MYR1.29 in FY19.

Offers a compelling dividend yield play

With a resilient balance sheet and healthy cashflows, Favelle has been able to reward its shareholders consistently with a decent dividend payment. We estimate Favelle to pay between 13.5 sen and 17 sen in DPS in FY19-21F, based on a 40% DPR. This translates into a compelling dividend yield of 5-6%, atypical in the capex intensive O&G industry, and which is also above the consumer sector's average dividend yield of 3%.

We do not rule out a higher dividend payment beyond that, for Favelle has the financial strength to pay out more without disrupting its working capital, capex and/ or potential inorganic growth.

Acquisition growth potential

Based on our estimates, Favelle offers a decent 3-year net profit CAGR of 13% (FY18-21E). What the market has yet to impute is the company's ample financial leverage to undertake any potential M&A exercises for inorganic growth. Its recent acquisition of a 70% stake on Exact Automation Group (Exact) for MYR91m fits well into its O&G portfolio. It contributes 18% of Favelle's order backlog. Similar to Favelle, Exact is net cash (MYR69m as at FY18). The acquisition is earnings accretive to the group, at an implied 6x FY18 PER.

Undemanding valuations

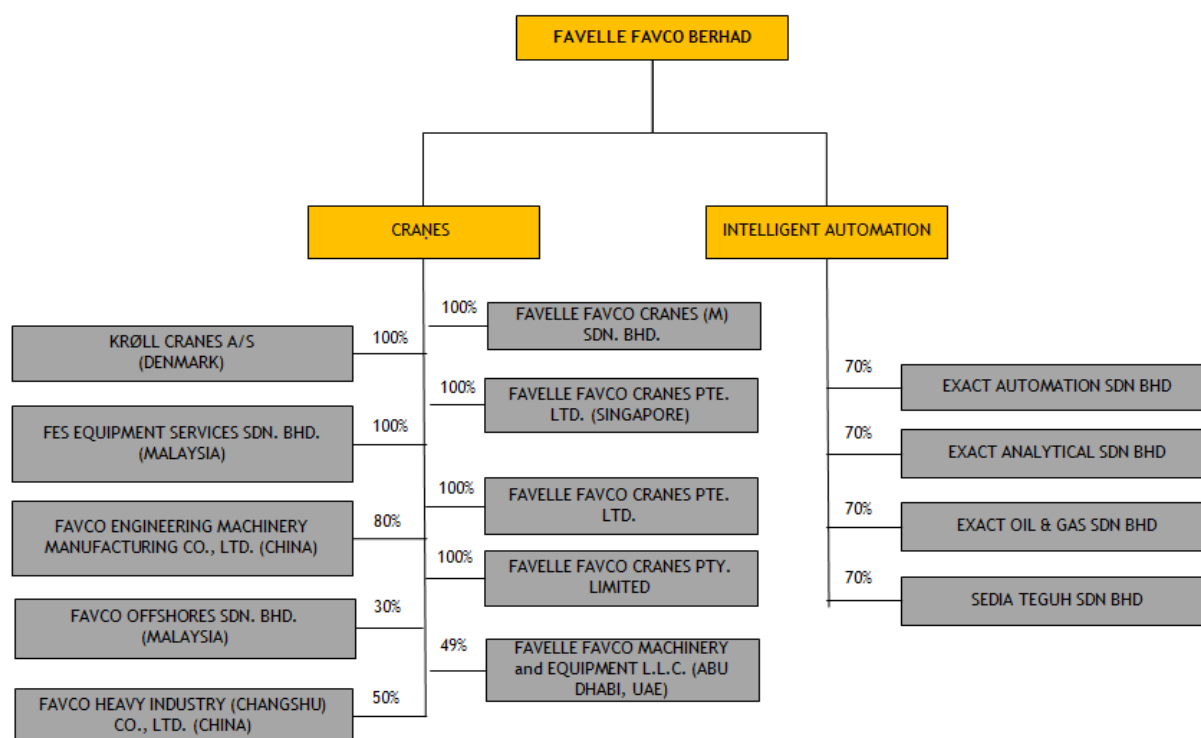
It trades at an undemanding 7x FY20 PER (4x PER ex-cash), 2x EV/ EBITDA and offers 5% in dividend yield vs. peers. At our TP, Favelle would offer a 30% upside (ex-dividend), which translates into 10x PER, 3x EV/ EBITDA and 4% dividend yield respectively. This is comparatively favourably against its global peers (see pg.16), which trade at higher multiple of 18x PER, 8x EV/ EBITDA and 0.5% dividend yield.

Corporate information

2 key divisions - cranes and automation

Favelle Favco (Favelle) has 2 key divisions, its: (i) crane manufacturing and (ii) intelligent automation businesses.

Fig 1: A snapshot of the group structure



Source: Company

#1: The cranes business - the history behind it

Favelle Favco was established in 1990 via the merger of EH Favelle Cranes and Favco. It was then acquired by Muhibbah Engineering (M) Bhd in 1995, which owns a 59.3% stake. It subsequently acquired Kroll Cranes A/S, Denmark in 1997 to further cement its position in the cranes business. Favelle was listed in 2006 at an IPO price of MYR0.55/shr.

Fig 2: Historical anecdotes of its cranes business

Year	Event
1990	EH Favelle Cranes and Favco merged to become Favelle Favco
1995	Favelle Favco bought over by Muhibbah Engineering (M) Bhd
1997	Favelle Favco acquires Kroll Cranes A/S
1998	Supplied its tower cranes to work on Petronas Twin Tower
2006	Favelle Favco went public on the 2 nd Board in August
2007	Successfully transferred to the Main Market

Source: Company

Favelle is predominantly a crane manufacturer (offshore, tower, wharf & crawler) with 7 operating facilities worldwide. It also offers rental, service & maintenance works of cranes.

Fig 3: Cranes: Revenue breakdown by operations

YE Dec	2013	2014	2015	2016	2017	2018
Revenue	764.2	797.9	792.4	582.3	526.5	457.7
- Construction	637.0	692.7	680.5	471.8	361.3	253.2
- Sales of spare parts	90.4	77.4	77.3	70.3	106.2	120.9
- Maintenance	36.8*	27.8*	34.7*	22.3	27.0	29.8
- Rental				17.9	32.1	53.9

Note: *No detailed breakdown

Source: Company

Comprising two international brands, Favelle and Kroll, the group is home to the largest hammerhead crane in the world, the Kroll K10,000 and the largest luffing tower crane in the world, the Favelle Favco M2480.

Its reputation for building the world's fastest cranes has cemented its position in the market for super high-rise buildings, having constructed 8 out of the world's 10 tallest buildings ever built to-date.

Fig 4: Manufacturing plants

Location	Senawang Malaysia	Copenhagen Denmark	Texas USA	Sydney Australia	Shanghai China
Current site area (m ²)	68,846	59,525	68,796	46,943	38,800
Built up (m ²)	16,986.6	12,889	6,000	8,607	4,000

Source: Company

Offshore cranes

- A pedestal-mounted elevating and rotating lifting device used to transfer materials and personnel to or from an offshore platform.
- Favelle offers 2 main series, rope luffing and ram luffing setups designed according to API 2C 7th Edition.
- Favelle can build both diesel-hydraulic and electro-hydraulic systems, demonstrating its capability to customize cranes according to a client's requirement and specification. This is presently their best seller.
- **Applications:** (i) Offshore platforms. (ii) jack-up barges, (iii) marine vessels and (iv) large submersibles

Tower cranes

- Probably the most common crane used in construction sites to lift building materials and equipment. Its fleet of tower cranes carries either the Favelle Favco or Kroll brand names.
- Favelle Favco's tower cranes (diesel hydraulic luffing cranes) are mainly engineered for heavy lifting and its standard range of lifting capacity varies from 60 to 2000 metre tonnes.
- Kroll cranes (electric hammerhead cranes) have a lifting capacity ranging from 70 to 25000 metre tonnes.

- Favelle introduced several new models in 2018 - tower crane luffing model MK220F, flattop tower cranes model K830F and K1230F. A total of 11 MK220F have been delivered to a client in Malaysia and this represents a breakthrough to penetrate into the smaller crane market.
- Applications:** (i) High rise structures, (ii) shipyards, (iii) power plants, (iv) bridges and (v) dams.

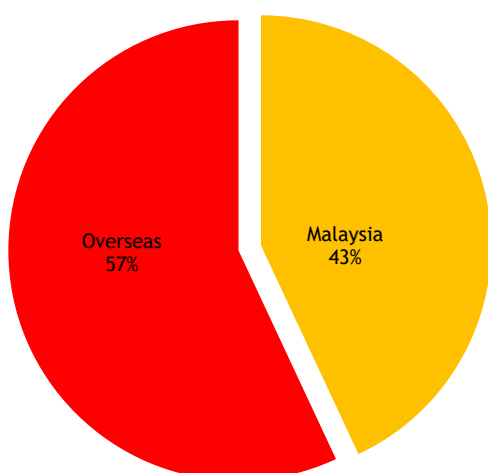
Crawler cranes

- A crawler crane is mounted on an under-carriage track and is able to travel through very rough landscapes.
- Its crawler crane range is jointly developed with Caterpillar Industrial Products Inc. (USA) and is a combination of Favelle Favco lifting technology and Caterpillar technology. It can be divided into telescopic boom and lattice boom.
- The cranes sizes range from 30 to 60 ton with a telescopic boom and 60 ton with a lattice boom. It is useful on worksites where mobility but not height is required.
- Applications:** (i) Construction sites and (ii) pipe laying works.

Wharf cranes

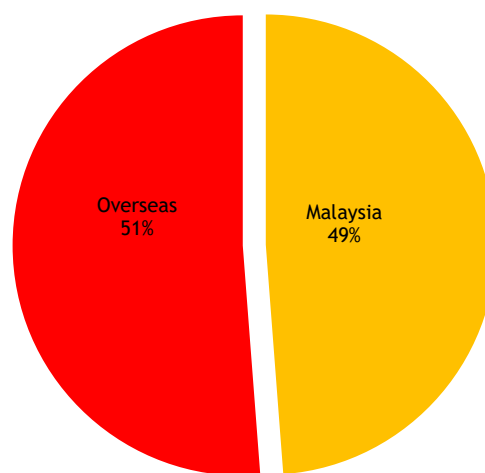
- A multipurpose wharf crane is primarily used in the shipyards and ports industry for a multitude of lifting tasks.
- Favelle offers both luffing and hammerhead cranes with diesel hydraulic and fully electric setups. It can be fitted with a hook, grab or spreader beam to handle materials or containers and is generally fitted with a travelling base to operate on a fast pace. Their innovative designs include level luffing bulk handling cranes.
- Applications:** (i) Shipyards, (ii) bulk handling terminals and (iii) general purpose terminals

Fig 5: Cranes: Revenue breakdown - by geography (2017)



Source: Company, Maybank KE

Fig 6: Cranes: Revenue breakdown - by geography (2018)



Source: Company, Maybank KE

Fig 7: Offshore crane, Azerbaijan, Shah Deniz II*Source: Company***Fig 8: Offshore crane, E-Drill-3, China***Source: Company***Fig 9: Wharf crane***Source: Company***Fig 10: Crawler crane***Source: Company***Fig 11: Tower crane, wind turbine instl***Source: Company***Fig 12: Tower crane, Russia, bridge to Russy Island***Source: Company***Fig 13: Port crane, J-25, Singapore***Source: Company*

#2: Intelligent automation business - a new segment

Exact Automation - an inorganic growth aspect. Favelle acquired a 70% stake in Exact Group (Exact) for MYR90.7m in Jul 2018. This was an earnings accretive deal, for the exercise was transacted at 1.4x EV/ EBITDA and 6x PER, based on its FY18 financials. This compares favourably against Favelle's own 2.5x and 7x respectively.

Earnings accretive, a good fit. This acquisition is a good fit to Favelle. Exact's management team's values are relatively comparable, in that they are cost conscious and very much bottomline-driven. Similar to Favelle, Exact is financially healthy, with net cash of MYR69m as at FY18. Based on historical financials, Exact's margins are superior vis-à-vis Favelle's.

All in, we expect Exact contribute about 18% to the Group's order backlog (MYR100m) and 14% to its bottomline.

Fig 14: Exact Group's selected financials

YE Dec (MYR'm)	2014	2015	2016	2017	2018
Revenue	107.6	91.8	107.2	129.3	116.5
EBITDA	31.7	31.7	21.2	23.7	25.4
Core net profit	22.3	15.7	14.0	20.1	20.6
Core net profit margin (%)	20.7	17.1	13.1	15.5	17.6
Net cash (MYR'm)	28.6	24.2	30.8	40.7	69.4

Source: Company

Fig 15: Margins: Cranes vs. automation

	2014	2015	2016	2017	2018
Gross margin (%)	22.4	27.6	24.3	28.5	33.3
- Cranes	22.4	27.6	24.3	28.5	33.3
- Automation	47.4	43.2	38.8	37.1	41.5
EBITDA margin (%)	17.1	26.9	20.3	22.1	24.6
- Cranes	17.1	26.9	20.3	22.1	24.6
- Automation	29.5	23.1	22.1	19.6	19.3
Pretax margin (%)	12.7	14.9	13.7	15.8	18.7
- Cranes	12.7	14.9	13.7	15.8	17.0
- Automation	28.3	21.7	19.3	18.6	29.0
Core NP margin (%)	13.1	22.5	16.1	15.2	14.1
- Cranes	13.1	22.5	16.1	15.2	14.1
- Automation	20.7	17.1	13.1	15.5	17.6

Source: Company

Fig 16: Exact Group's activities

Name	Principal activities
Exact Automation	<ul style="list-style-type: none"> Trading of: (i) industrial IT equipment and (ii) automation & control components for power, quality measurement. Provision of integrated industrial automation solutions on the design, engineering, testing and project management of plant instrumentation as well as its related maintenance services.
Exact Analytical	<ul style="list-style-type: none"> Trading of process analyzers, continuous emission monitoring systems. Provides engineering services on installation, commissioning, maintenance of environmental & process analyzers.
Exact Oil & Gas	<ul style="list-style-type: none"> Trading and engineering of specialized equipment used in the O&G industry. This includes the calibration, verification, installation, commissioning, repairs and maintenance of the equipment and systems.
Sedia Teguh	<ul style="list-style-type: none"> Trading of specialized equipment used in the O&G industry including calibration, verification, installation, commissioning, repairs and maintenance of control meters.

Source: Company

Exact's business in a nutshell. Exact's businesses include automation, control & instrumentation, rotating machinery systems, renewable energy systems, gas/liquid analysis systems, valves automation and industrial information digital systems. It currently holds more than 20 active maintenance contracts established with most of the oil majors in Malaysia.

Exact provides integrated design, engineering, testing, calibration, verification, installation, commissioning of automation process solution trading, repairs & maintenance for:

- Industrial automation solutions & project management of plant instrumentation;
- Specialised equipment for the O&G industry;
- Environmental and process analysers; and
- Continuous emission monitoring systems.

As the trend towards cleaner air and environmentally friendly industrial plants develops, this division is riding the wave with several notable projects. This includes the delivery of a Vapour Recovery Unit (VRU), the 1st VRU project that complies with the Department of Environment's (DOE) stringent regulations on volatile organic compound emission limits.

As part of PETRONAS' digitalization efforts, Favelle was awarded a 2-year PRIME Integrated Operations contract, which is an initiative to address the needs for a predictive approach in instrument reliability and availability.

Fig 17: Exact's financials by companies

YE Dec	2014	2015	2016	2017	2018
Revenue (MYR'm)	107.6	91.8	107.2	129.3	116.5
- Exact Automation	65.6	52.8	55.2	66.1	78.6
- Exact Analytical	15.7	21.8	23.3	16.8	18.9
- Exact Oil & Gas	3.7	9.9	8.9	8.9	5.8
- Sedia Teguh	112.6	71.2	85.3	103.8	105.2
- Inter-co elimination	-90.1	-63.9	-65.4	-66.4	-92.0
Gross profit (MYR'm)	51.0	39.7	41.6	48.0	48.3
- Exact Automation	31.9	24.7	26.3	30.7	33.0
- Exact Analytical	6.2	7.2	7.8	5.8	6.5
- Exact Oil & Gas	0.5	0.8	1.1	2.1	-0.8
- Sedia Teguh	12.5	7.0	6.5	9.4	9.7
EBITDA (MYR'm)	31.7	21.2	23.7	25.4	22.4
- Exact Automation	22.0	14.7	17.0	17.6	16.3
- Exact Analytical	2.9	3.3	3.3	1.3	0.8
- Exact Oil & Gas	0.2	0.2	0.2	1.4	-0.9
- Sedia Teguh	6.6	3.1	3.2	5.0	6.2
Exceptional items (MYR'm)	0.4	-0.8	1.3	-0.8	0.9
- Exact Automation	0.4	0.0	1.1	-0.7	-0.3
- Exact Analytical	0.0	0.0	0.0	-0.1	0.5
- Exact Oil & Gas	0.0	0.0	0.0	0.0	0.5
- Sedia Teguh	-0.1	-0.8	0.2	-0.1	0.2
Pretax profit (MYR'm)	30.4	19.9	20.7	24.1	27.5
- Exact Automation	21.4	14.1	16.5	16.9	16.8
- Exact Analytical	2.7	3.0	3.2	1.0	1.2
- Exact Oil & Gas	0.2	0.1	0.2	1.4	3.4
- Sedia Teguh	6.1	2.7	0.8	4.7	6.2

Exact's financials by companies (continued)

YE Dec	2014	2015	2016	2017	2018
Net profit (MYR'm)	22.7	14.9	15.3	19.2	21.4
- Exact Automation	16.0	10.7	12.3	13.2	12.3
- Exact Analytical	2.1	2.2	2.5	0.6	1.1
- Exact Oil & Gas	0.1	0.1	0.2	1.4	3.4
- Sedia Teguh	4.5	1.9	0.3	4.0	4.7
Core net profit (MYR'm)	22.3	15.7	14.0	20.1	20.6
- Exact Automation	15.6	10.7	11.2	13.9	12.6
- Exact Analytical	2.0	2.2	2.5	0.7	0.6
- Exact Oil & Gas	0.1	0.1	0.2	1.4	2.9
- Sedia Teguh	4.6	2.7	0.1	4.1	4.5
Net cash / (debt)	28.6	25.2	31.6	39.9	59.6
- Exact Automation	13.7	12.5	17.6	29.6	37.6
- Exact Analytical	4.2	1.0	1.9	1.4	2.9
- Exact Oil & Gas	0.4	0.5	0.8	0.7	1.2
- Sedia Teguh	10.3	11.2	11.3	8.2	18.0
Margins (%)					
Gross profit margin (%)	47.4	43.2	38.8	37.1	41.5
- Exact Automation	48.6	46.8	47.6	46.4	41.9
- Exact Analytical	39.2	33.0	33.4	34.6	34.6
- Exact Oil & Gas	14.0	7.8	12.0	23.7	-14.3
- Sedia Teguh	11.1	9.9	7.6	9.0	9.2
EBITDA margin (%)	29.5	23.1	22.1	19.6	19.3
- Exact Automation	33.6	27.8	30.9	26.6	20.7
- Exact Analytical	18.8	14.9	14.3	7.6	4.5
- Exact Oil & Gas	4.2	1.5	2.3	16.2	-15.4
- Sedia Teguh	5.8	4.4	3.7	4.9	5.9
Pretax profit margin (%)	28.3	21.7	19.3	18.6	29.0
- Exact Automation	32.7	26.7	29.9	25.6	21.3
- Exact Analytical	17.5	13.5	13.7	6.2	6.1
- Exact Oil & Gas	4.1	1.5	2.3	16.1	58.6
- Sedia Teguh	5.4	3.9	0.9	4.5	5.9
Net profit margin (%)	21.1	16.2	14.2	14.9	18.4
- Exact Automation	24.4	20.3	22.3	20.0	15.6
- Exact Analytical	13.1	9.9	10.6	3.7	5.7
- Exact Oil & Gas	3.3	1.2	2.0	15.6	58.6
- Sedia Teguh	4.0	2.7	0.4	3.9	4.5
Core net profit margin (%)	20.7	17.1	13.1	15.5	17.6
- Exact Automation	23.7	20.3	20.4	21.0	16.0
- Exact Analytical	12.8	9.9	10.6	4.0	3.2
- Exact Oil & Gas	3.3	1.2	2.0	16.2	50.6
- Sedia Teguh	4.1	3.8	0.1	3.9	4.2

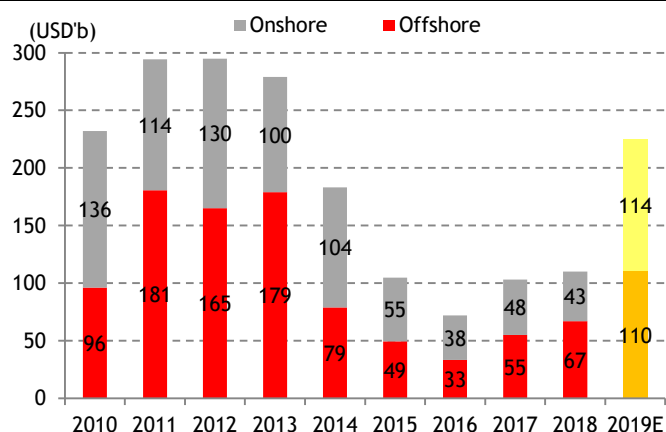
Source: Company

O&G: Prospect & outlook

The offshore market is set for a resurgence, with global sanctioning of projects on a rapid rise.

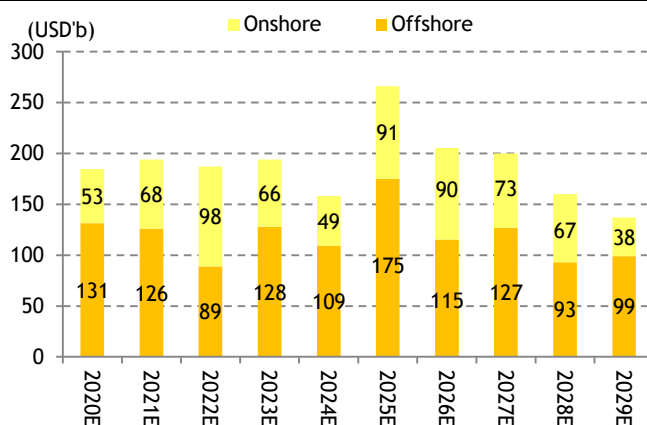
- According to Rystad Energy research, commitments for new offshore projects will grow from USD67b in 2018 to USD110b in 2019. Of the USD110b, 61% has been sanctioned to-date.
- Based on a bottom-up mapping of the future line-up of projects, greenfield capex is rising exponentially, with an estimated capex of USD120b p.a. (average) in 2019-21. The trough-to-peak capex range over the last seven years was between USD40b in 2016 and USD180b in 2013.
- The global offshore crane market is expected to reach USD26b by 2022 growing at a CAGR of 9.9%, according to Statistics MRC.

Fig 18: Greenfield project commitments (2010-2019E)



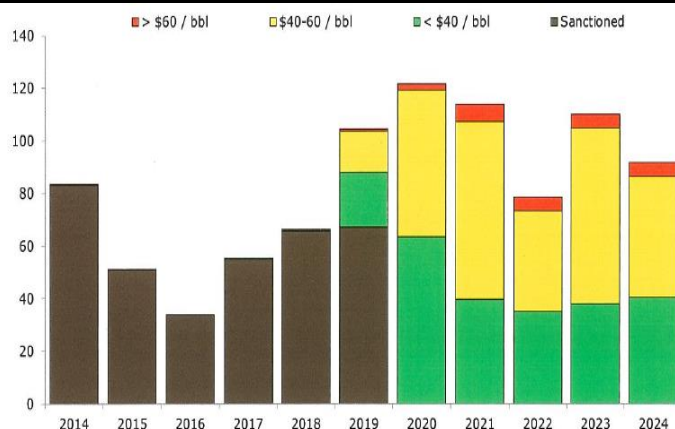
Source: Rystad Energy research and analysis, ServiceCube

Fig 19: Greenfield project commitments (2020-2029E)



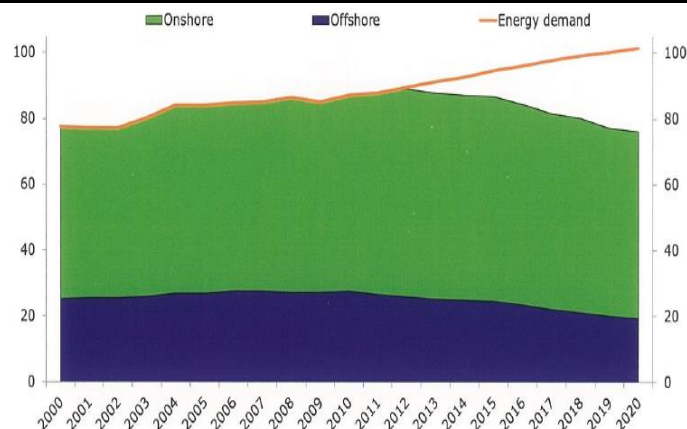
Source: Rystad Energy research and analysis, ServiceCube

Fig 20: Offshore commitments by breakeven oil price



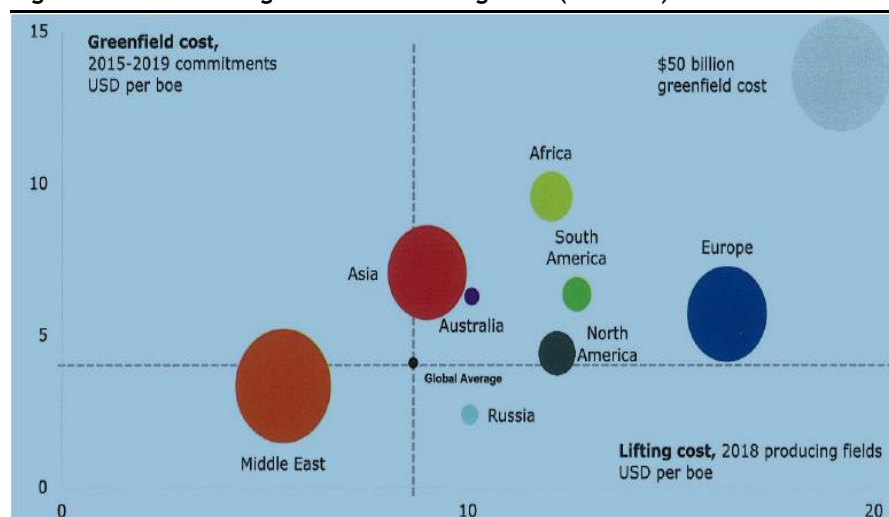
Source: Rystad Energy research and analysis, ServiceCube

Fig 21: Additional SS to meet global energy DD (m bpd)



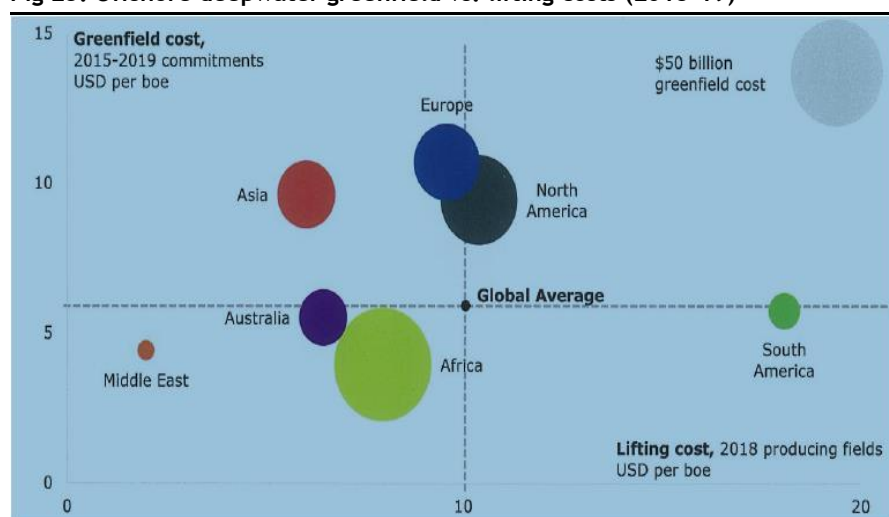
Source: Rystad Energy research and analysis, ServiceCube

Fig 22: Offshore shelf greenfield vs. lifting costs (2015-19)



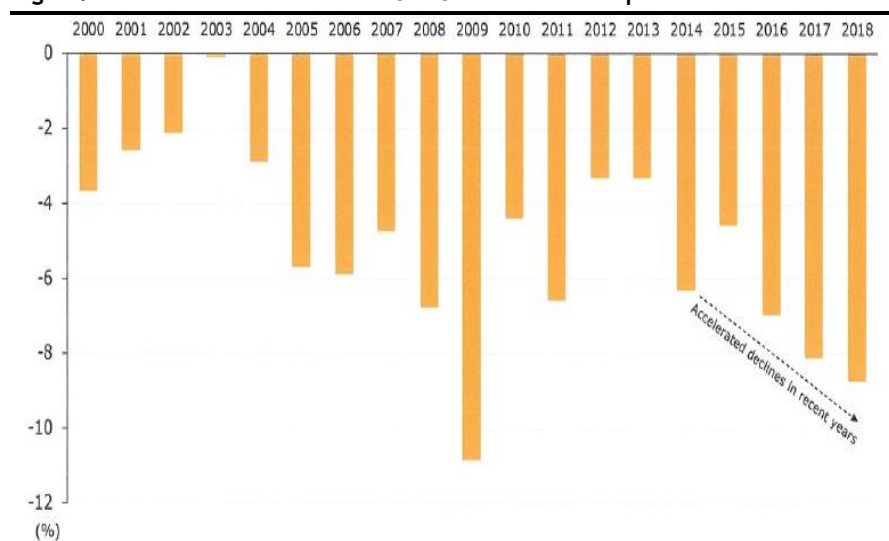
Source: Rystad Energy research and analysis, ServiceCube

Fig 23: Offshore deepwater greenfield vs. lifting costs (2015-19)



Source: Rystad Energy research and analysis, ServiceCube

Fig 24: YoY % fall in offshore non-OPEC mature fields* production



Note: * Fields started up before 1995

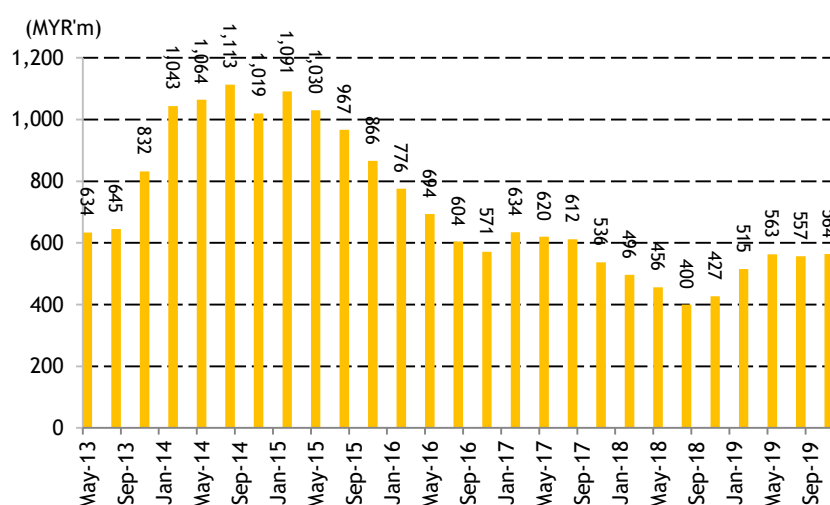
Source: Rystad Energy research and analysis, ServiceCube

Financial analysis and forecasts

Favelle's business is predominantly orderbook driven. About 80% of its order backlog is typically cranes related (with automation making up the rest) and it is cyclically exposed to the offshore O&G activities. Orderbook visibility is typically of a 12-month range.

Orders on the cyclical rise. Having bottomed at MYR400m in May 2018, its order backlog is gradually on a cyclical revival. In fact, it has started to experience a pick-up in its cranes orders, up +26% YoY to MYR464m (ex-automation's MYR100m) as at Nov 2019. That said, it offers further upside, for it is still below its peak level of MYR1.1b in May 2014.

Fig 25: Favelle: Order backlog (cranes & automation)



Source: Company

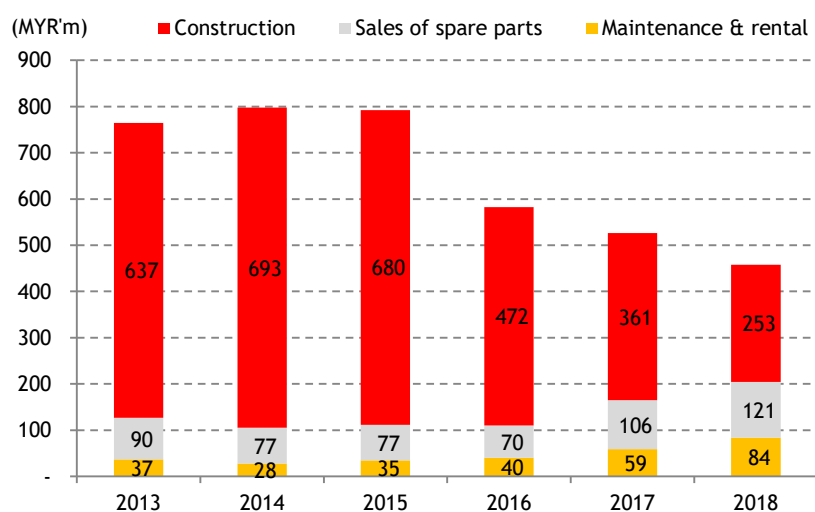
Cranes maintenance and rental business have ample room to grow. While Favelle has been predominantly a crane manufacturer, its maintenance and rental aspects are picking up. We view this very positively, for it offers Favelle a steady, stable and recurring income stream.

Fig 26: Cranes maintenance & rental services relative to revenue

	2013	2014	2015	2016	2017	2018
Revenue - cranes (LHS)	764.2	797.9	792.4	582.3	526.5	457.7
- % of maintenance & rental services to cranes revenue	4.8	3.5	4.4	6.9	11.2	18.3
- % of maintenance & rental services to Group's revenue	4.8	3.5	4.4	6.9	11.2	15.8

Source: Company

Fig 27: Maintenance & rental business relative to its cranes revenue



Source: Company

3-year revenue/ net profit CAGR of 13%. We expect Favelle's order backlog for cranes operations to grow to MYR600m-MYR800m in FY19-21E, a realistic target in our view. As for its automation operations, we expect a steady flow of MYR70m-90m or new orders p.a.

Putting things into perspective, we expect Favelle to register a 3-year revenue/ net profit CAGR of 13% (FY18-21E) respectively. Its cranes business will lead the group's earnings growth with its 70%-owned automation operations delivering about 14% of its net profit in FY19-21.

Fig 28: Favelle: Segmental financial breakdown

	2017	2018	2019F	2020F	2021F
Revenue (MYR'm)	526.5	530.6	620.0	690.7	758.0
- Cranes	526.5	457.6	540.0	600.0	660.0
- Automation	0.0	73.0	80.0	90.7	98.0
Pretax profit (MYR'm)	83.3	99.0	104.9	116.7	130.0
- Cranes	83.3	77.8	84.9	94.2	105.5
- Automation	NM	21.2	20.0	22.6	24.5
Pretax margin (%)					
- Cranes	15.8	17.0	15.7	15.7	16.0
- Automation	NM	29.0	25.0	25.0	25.0

Source: Maybank KE

Balance sheet & FCFs

An atypical O&G stock. Business-wise, as an orderbook-driven engineering & construction O&G company, we are impressed by its ability to generate cash, preserve capital and maintain a net cash company.

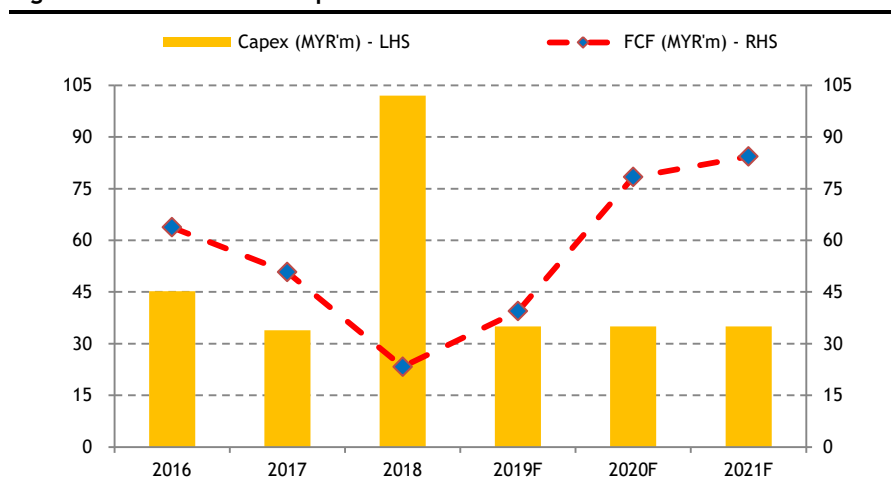
Resilient balance sheet. Favelle is one of the few that has been consistently generating strong FCFs. More importantly, it has also proven to be financially resilient during the downcycle, being profitable through the 2015-18 period.

Strong cash generative proposition. Even with its significant acquisition last year (MYR91m on 70% Exact), Favelle remained in a net cash position. Its net cash stood at MYR220m (@MYR0.99/shr) as at Nov 2019.

Can seek an inorganic growth route, should the opportunity arise. Its strong balance sheet offers Favelle an avenue to prospect for compelling acquisition targets to deliver inorganic growth. Our forecasts do not incorporate any such potential just yet.

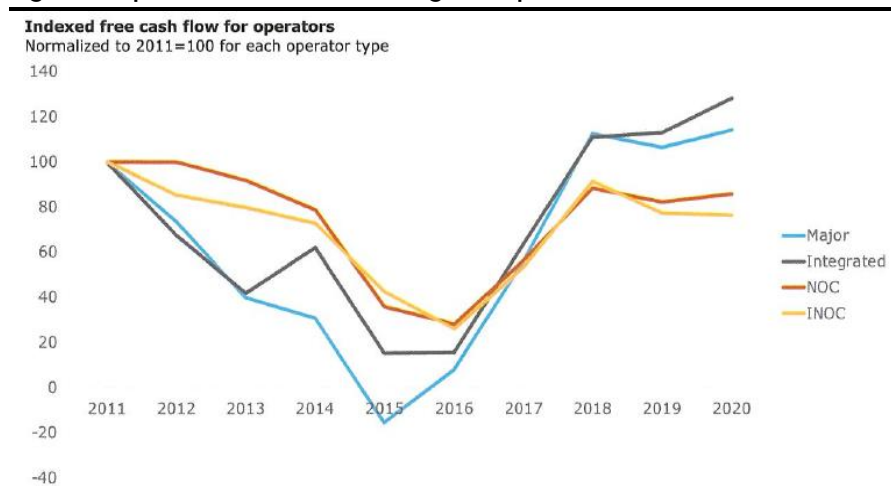
Financially, we expect its cash position to improve, on the back of rising FCFs of MYR39m-84m over the next 3 years. We estimate a steady state capex of MYR35m p.a., mainly for maintenance related purposes.

Fig 29: Favelle: FCFs vs. capex



Source: Maybank Kim Eng

Fig 30: Snapshot of indexed FCFs for global operators



Source: Rystad Energy research and analysis, UCube

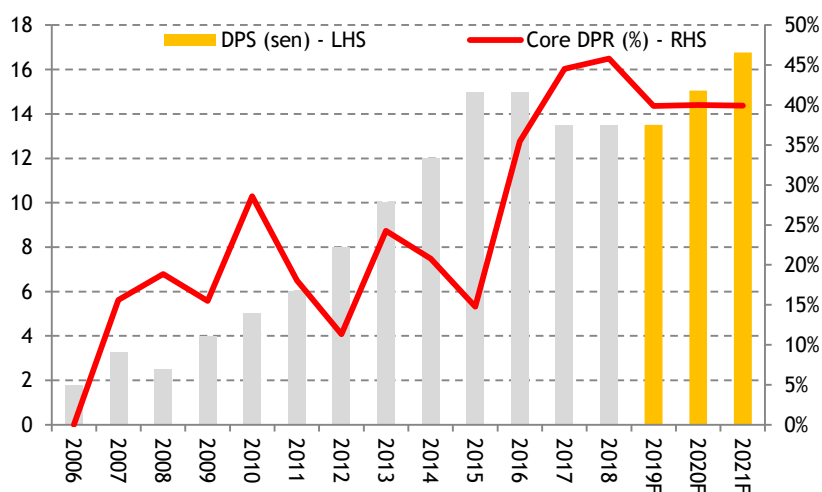
Dividends

Consistently has paid decent dividends. While Favelle has no firm dividend policy, it has consistently paid out between 13.5 sen and 15 sen p.a. in DPS (35%-46% DPR) over the last 3 years. This is despite the O&G market going through a cyclical downturn (2016-18).

With attractive dividend yields; above the consumer sector's average. The DPS translates into a decent dividend yield of 5%, which is atypical in the capex-intensive O&G sector.

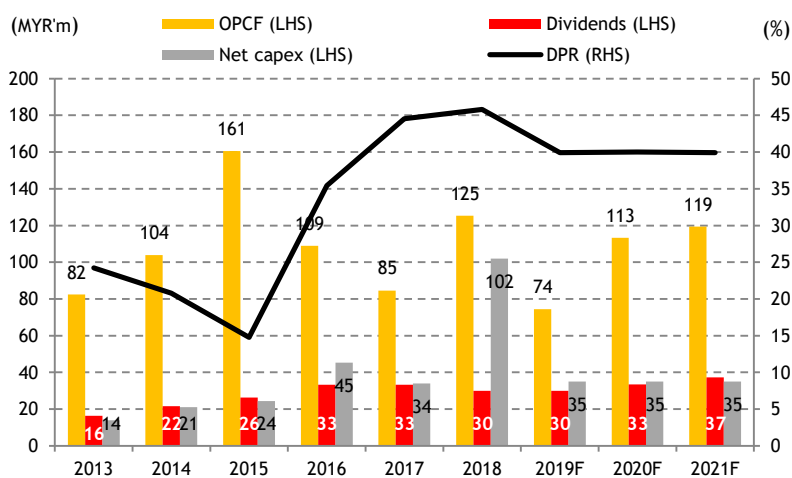
40% dividend payout with room to grow. While we conservatively expect Favelle to maintain its 13.5sen DPS in FY19, we do not rule out a higher payout in the future, in view of its strong FCFs. At a 40% DPR, Favelle should be able to declare 15-17 sen DPS in FY20-21, based on our estimate.

Fig 31: Favelle: DPS vs. DPR



Source: Company, Maybank KE

Fig 32: Dividend payouts well supported by FCF



Source: Company, Maybank KE

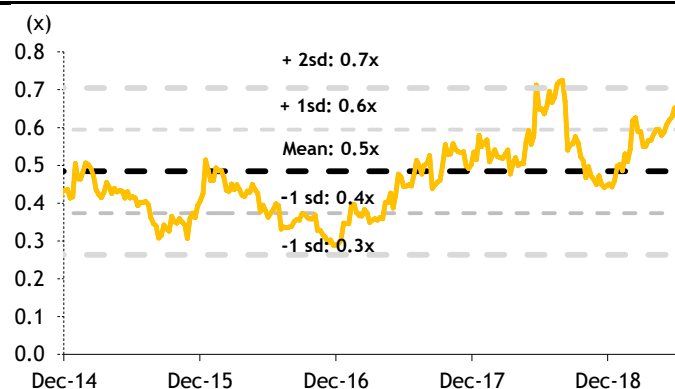
Valuations

We initiate coverage on Favelle with a BUY and MYR3.65 TP. Our valuation is pegged to 0.6x EV/ order backlog. Our 0.6x EV assumption is based on its 5-year +1 SD valuation while the MYR725m orders are premised on its average revenue for FY20-21.

We prefer this valuation method over others (i.e. PER, EV/EBITDA, P/BV, DDM) for its captures the cyclical nature of Favelle's orderbook and takes into account its balance sheet/ cashflows strength.

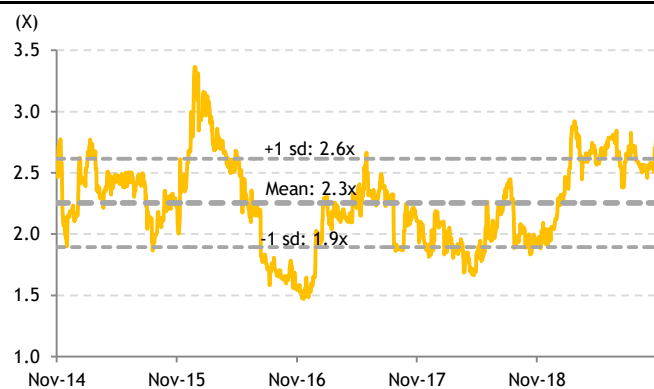
Putting things into perspective, our TP implies 9.7x PER, 6.2x PER (ex-cash), 3.4x EV/EBITDA, 1x P/BV and 4.1% dividend yield for FY20, which is undemanding vis-à-vis its peers.

Fig 33: Favelle: 12M forward EV/ order backlog trend



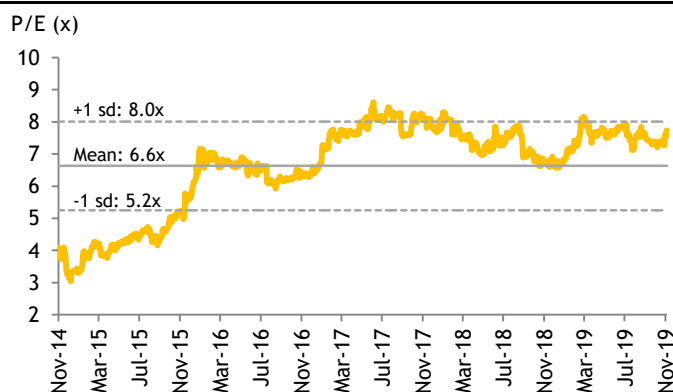
Source: Maybank KE

Fig 34: Favelle: 12M forward EV/ EBITDA trend



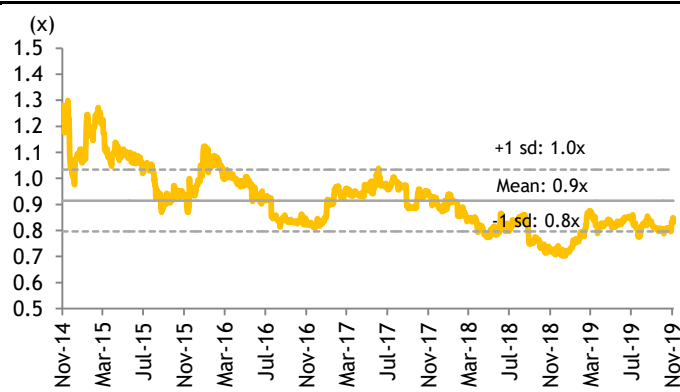
Source: Maybank KE

Fig 35: Favelle: 12M forward PER band



Source: Maybank KE

Fig 36: Favelle: 12M forward PBV band



Source: Maybank KE

Fig 37: Peer comparisons

		Price	Mkt cap	PER (x)		EV/ EBITDA (x)		PBV (x)		Div. Yield (%)	
		(USD)	(USD'm)	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Manitowoc	MTW US	15.57	550.4	8.5	10.6	5.4	6.2	0.9	0.8	0.0	0.0
National	NOV US	22.09	8,523.0	NM	24.7	13.0	10.7	0.9	0.9	0.9	0.9
				=====	=====	=====	=====	=====	=====	=====	=====
Simple avg.				NM	17.6	9.2	8.4	0.9	0.8	0.5	0.5

Source: Bloomberg

Key risk factors

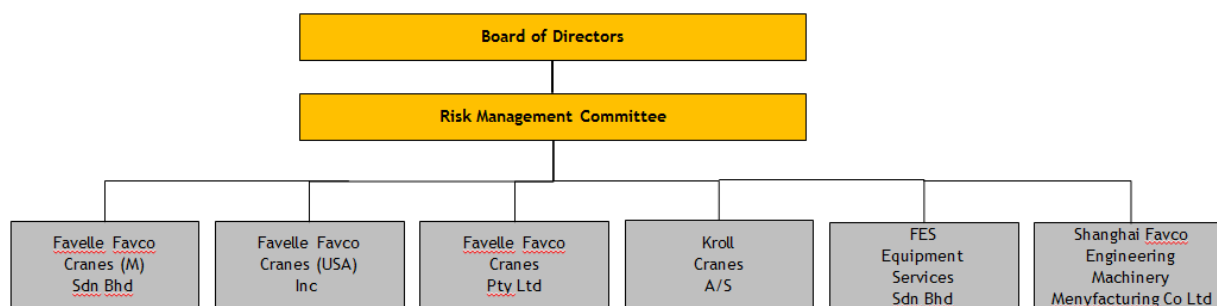
Contract award delays. Favelle's order book is dependent on offshore oil & gas field developments and onshore construction works. These are subject to planning, regulatory and political hurdles, which can delay field development and awards to fabricate offshore structures.

Oil price levels affect long term investment plans. Oil majors' investment plans are dependent on long-term oil price assumptions, which can be affected by low and/or volatile oil price levels.

We have seen oil field exploration/developments shelved when oil price fell below USD50/bbl (average) in 2008/ 2015, and there is no certainty this will not recur. Our economics team projects an average USD60/bbl crude oil price in 2020 (2019: USD63/bbl).

Margin squeeze from cost inflation. Labour, one of Favelle's major cost items, generally suffers from long-term upward cost pressure while steel is a volatile cost item. The latter is usually passed on to customers in cost-plus clauses in contracts.

Organizational Chart



Source: Annual Report

Board of directors & key management

Name	Designation	Experience
Tan Sri A. Razak bin Ramli	Chairman, Senior Independent Non-Executive Director	<ul style="list-style-type: none"> Obtained a Bachelor of Arts (Honours) degree majoring in Public Administration from the University of Tasmania in 1971 and holds a Diploma (Gestion Publique) from the Institut Internationale d'Administration Publique, Paris (1980). He is the Chairman of Shangri-La Hotels (Malaysia) Berhad.
Tan Sri Dato' Seri Ahmad Ramli bin Haji Mohd Nor	Vice Chairman, Independent Non-Executive Director	<ul style="list-style-type: none"> Holds a Master's Degree in Public Administration from Harvard University, USA. He is a Director of several private limited companies and is also a Director of Affin Islamic Bank Berhad and Boustead Heavy Industries Corporation Bhd. He retired as the Chief of the Royal Malaysian Navy in January 1999. During his 35 years of service in the Navy, he received numerous awards, both local and international.
Mac Chung Hui	Managing Director/Chief Executive Officer	<ul style="list-style-type: none"> He holds a Bachelor of Civil Engineering degree from the University of Nottingham, UK. He has been overseeing the production and operation of Favelle Favco Cranes Pty Limited and Favelle Favco Cranes (M) Sdn Bhd over the past eighteen years.
Mac Ngan Boon @ Mac Yin Boon	Executive Director	<ul style="list-style-type: none"> Obtained a Bachelor of Engineering (Civil) degree from the University of Western Australia in 1967. He is a professional engineer and a member of the Institute of Engineers Malaysia. He has been the Chairman of the Machinery and Equipment Manufacturers Association of Malaysia (MEMA) since 1998 and the Chairman of Machinery and Engineering Industries Federation (MEIF) since 2016.
Shirleen Lee Poh Kwee	Executive Director	<ul style="list-style-type: none"> A qualified Chartered Accountant with the Malaysian Institute of Accountants, a Fellow Member of the ACCA, United Kingdom, and a Certified Financial Planner of the Financial Planning Association of Malaysia. Prior to joining Muhibbah as a Group Financial Controller in 1993, she was attached to KPMG Malaysia, for 4 years. She is currently the Group Finance Director of Muhibbah.
Mazlan bin Abdul Hamid	Executive Director	<ul style="list-style-type: none"> Executive Director of Favelle and heads the Marketing & Business Development. He is also a Director of FFM, Favco Offshores Sdn Bhd, Exact Automation Sdn Bhd, Exact Analytical Sdn Bhd, Exact Oil & Gas Sdn Bhd, Sedia Teguh Sdn Bhd and Muhibbah Marine Engineering. Obtained a Diploma in Engineering from the University of Mara Technology in 1984 and attended an Advanced Metallurgy course in the United Kingdom in 1985. In the same year, he started his career as a project coordinator in DNT (M) Sdn Bhd. He then joined SCS Petrotechnical (M) Sdn Bhd and was seconded to Sarawak Shell Berhad, and thereafter, he joined Bureau Veritas (M) Sdn Bhd as Surveyor and Marketing Manager.
Sobri bin Abu	Independent Non-Executive Director	<ul style="list-style-type: none"> His career spans for more than thirty years in the O&G industry, with major international oil companies, namely ExxonMobil and PETRONAS as well as engineering construction companies like Babcock King Wilkinson, Stone and Webster Engineering Construction, Petrofac, Sumatec Engineering and Ranhill WorleyParsons.
Dato' Sri Khazali bin Haji Ahmad	Independent Non-Executive Director	<ul style="list-style-type: none"> He graduated with a Bachelor of Economics degree from National University of Malaysia in 1980 and received a Master's Degree in Economics from the University of Central Oklahoma. He was posted to the International Trade Division of the Ministry of International Trade and Industry (MITI), Tax Analysis Division under the Ministry of Finance, and became Section Chief in the Division, served as Special Functions Officer to the Chief Secretary to the Government in the Prime Minister's Department, Director General of Customs.

Source: Company

FYE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Key Metrics					
P/E (reported) (x)	9.6	8.7	8.3	7.4	6.7
Core P/E (x)	8.1	7.8	8.3	7.4	6.7
P/BV (x)	1.0	0.8	0.9	0.8	0.8
P/NTA (x)	1.0	0.9	1.0	0.9	0.8
Net dividend yield (%)	4.9	5.9	4.8	5.4	6.0
FCF yield (%)	8.4	4.6	6.3	12.6	13.6
EV/EBITDA (x)	2.5	2.5	2.9	2.4	1.9
EV/EBIT (x)	3.1	3.1	3.6	2.8	2.2

INCOME STATEMENT (MYR m)

Revenue	526.5	530.6	620.0	690.7	758.0
Gross profit	150.1	176.8	204.6	227.9	250.1
EBITDA	106.3	106.5	127.2	138.5	151.9
Depreciation	(20.4)	(21.0)	(23.6)	(23.6)	(23.6)
Amortisation	(0.1)	(0.1)	0.0	0.0	0.0
EBIT	85.7	85.3	103.6	114.9	128.3
Net interest income / (exp)	5.1	3.9	4.3	4.8	4.7
Associates & JV	(0.8)	(2.6)	(3.0)	(3.0)	(3.0)
Exceptionals	(11.5)	(1.9)	0.0	0.0	0.0
Other pretax income	(4.0)	(3.0)	(2.0)	(1.0)	0.0
Pretax profit	83.3	99.0	104.9	116.7	130.0
Income tax	(19.3)	(30.4)	(25.2)	(28.0)	(31.2)
Minorities	(0.9)	(5.3)	(4.6)	(5.2)	(5.6)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	63.1	63.3	75.2	83.5	93.2
Core net profit	74.6	65.2	75.2	83.5	93.2

BALANCE SHEET (MYR m)

Cash & Short Term Investments	372.1	323.8	332.1	379.3	429.2
Accounts receivable	200.0	213.1	238.5	265.7	291.5
Inventory	156.5	164.1	238.5	215.9	236.9
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	241.8	333.9	345.3	356.7	368.1
Intangible assets	0.2	71.3	71.3	71.3	71.3
Investment in Associates & JVs	14.7	12.2	9.2	6.2	3.2
Other assets	222.1	162.2	162.2	162.2	162.2
Total assets	1,207.4	1,280.6	1,397.0	1,457.2	1,562.4
ST interest bearing debt	15.1	24.0	24.0	24.0	24.0
Accounts payable	232.9	258.6	326.3	328.9	369.7
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	18.8	23.1	22.0	20.9	19.8
Other liabilities	312.0	285.0	285.0	285.0	285.0
Total Liabilities	579.2	590.8	657.4	658.9	698.7
Shareholders Equity	629.5	659.7	705.0	758.5	818.3
Minority Interest	(1.3)	30.1	34.7	39.8	45.4
Total shareholder equity	628.2	689.8	739.7	798.4	863.8
Total liabilities and equity	1,207.4	1,280.6	1,397.0	1,457.2	1,562.4

CASH FLOW (MYR m)

Pretax profit	83.3	99.0	104.9	116.7	130.0
Depreciation & amortisation	20.5	21.1	23.6	23.6	23.6
Adj net interest (income)/exp	0.0	0.0	0.0	0.0	0.0
Change in working capital	(33.1)	(11.1)	(32.0)	(2.0)	(6.1)
Cash taxes paid	(19.3)	(30.4)	(25.2)	(28.0)	(31.2)
Other operating cash flow	32.3	44.1	0.0	0.0	0.0
Cash flow from operations	84.6	125.3	74.4	113.3	119.3
Capex	(33.9)	(102.0)	(35.0)	(35.0)	(35.0)
Free cash flow	50.7	23.3	39.4	78.3	84.3
Dividends paid	(33.2)	(29.9)	(30.0)	(33.4)	(37.2)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	(3.6)	(1.7)	(1.2)	(1.1)	(1.0)
Other invest/financing cash flow	(8.6)	(1.6)	0.1	3.4	3.8
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	5.3	(10.0)	8.3	47.2	49.9

FYE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
Key Ratios					
Growth ratios (%)					
Revenue growth	(9.6)	0.8	16.9	11.4	9.7
EBITDA growth	7.3	0.2	19.5	8.9	9.7
EBIT growth	7.2	(0.4)	21.4	10.9	11.7
Pretax growth	4.4	18.9	6.0	11.2	11.4
Reported net profit growth	(15.5)	0.4	18.7	11.1	11.6
Core net profit growth	(20.4)	(12.5)	15.2	11.1	11.6
Profitability ratios (%)					
EBITDA margin	20.2	20.1	20.5	20.1	20.0
EBIT margin	16.3	16.1	16.7	16.6	16.9
Pretax profit margin	15.8	18.7	16.9	16.9	17.2
Payout ratio	47.4	47.2	39.9	40.0	39.9
DuPont analysis					
Net profit margin (%)	12.0	11.9	12.1	12.1	12.3
Revenue/Assets (x)	0.4	0.4	0.4	0.5	0.5
Assets/Equity (x)	1.9	1.9	2.0	1.9	1.9
ROAE (%)	10.3	9.8	11.0	11.4	11.8
ROAA (%)	6.3	5.2	5.6	5.9	6.2
Liquidity & Efficiency					
Cash conversion cycle	72.6	53.2	52.1	53.2	45.1
Days receivable outstanding	150.8	140.1	131.1	131.4	132.3
Days inventory outstanding	142.3	163.1	174.4	176.7	160.5
Days payables outstanding	220.5	250.0	253.4	254.9	247.6
Dividend cover (x)	2.1	2.1	2.5	2.5	2.5
Current ratio (x)	1.7	1.5	1.5	1.6	1.7
Leverage & Expense Analysis					
Asset/Liability (x)	2.1	2.2	2.1	2.2	2.2
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	na	na	na	na	na
Debt/EBITDA (x)	0.3	0.4	0.4	0.3	0.3
Capex/revenue (%)	6.4	19.2	5.6	5.1	4.6
Net debt/ (net cash)	(338.2)	(276.6)	(286.1)	(334.4)	(385.4)

Source: Company; Maybank

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