

3QFY18 RESULTS UPDATE

28 Nov 2018

Favelle Favco Bhd

Price : RM2.25

Market Capitalization : RM498.2 mln

Market : Main Market

Sector : Industrial Products

Recommendation : Buy

Bursa / Bloomberg Code: 7229 / FFB MK
Stock is Shariah-compliant.

Favco: 3QFY18 results

FYE Dec (RM mln)	Quarter-on-Quarter			Year-on-Year		Cumulative		
	3QFY18	2QFY18	% chg	3QFY17	% chg	9MFY18	9MFY17	% chg
Revenue	164.6	89.8	83.2%	168.2	-2.1%	356.6	433.5	-17.7%
Operating profit	41.1	11.4	262.2%	27.0	52.5%	60.7	65.1	-6.8%
Finance costs	(0.4)	(0.2)		(0.2)		(0.8)	(0.6)	
Pre-tax profit	40.8	11.1	265.6%	26.8	52.4%	59.9	64.6	-7.2%
Tax	(9.1)	(3.4)		(6.4)		(15.1)	(11.6)	
Net profit	30.1	7.3	314.8%	20.1	49.5%	42.8	52.4	-18.2%
Reported EPS (sen)	13.6	3.3	314.8%	9.1	49.5%	19.4	23.7	-18.2%
Op. profit margin	25.0%	12.6%		16.0%		17.0%	15.0%	
Pre-tax margin	24.8%	12.4%		15.9%		16.8%	14.9%	
Net profit margin	18.3%	8.1%		12.0%		12.0%	12.1%	
Net assets/share (RM)	3.0							

3QFY18 Results Review

- Favco's 3QFY18 net profit jumped 49.5% YoY to RM30.1 mln, boosting 9MFY18 net profit to RM42.8 mln. The reported net profit constituted 82.7% of our earnings estimates. Meanwhile, the reported 9MFY18 revenue at RM356.6 mln also exceeded our expectations, making up 83.0% of our estimates.
- Analysis of the geographical breakdown showed that the sharp improvement in 3QFY18 net profit was due to contribution from the consolidation of Exact Group that was acquired in July 2018. Favco's local sales (including of Exact Group's contribution of RM26.0 mln) made up 47.0% of the Group's total revenue of RM164.6 mln in 3QFY18. Contribution from overseas, meanwhile, stood at RM87.2 mln, accounting for the balance 53.0% of the Group revenue in 3QFY18.
- Nevertheless, despite the robust 3QFY18 performance, the sluggish performance earlier in 1HFY18 resulted in the Group's 9MFY18 revenue decreasing 17.7% YoY to RM356.6 mln. In tandem with the lower turnover, 9MFY18 net profit too contracted by 18.2% YoY to RM42.8 mln. Contribution from overseas continued to anchor the Group's performance, contributing some 60.5% to top line in 9MFY18. Although both the top and bottom lines were lower YoY, we note that Favco's net profit margin remained relatively healthy, hovering at 12.0% in 9MFY18, just marginally higher against the five-year average historical net profit margin at 11.3%.
- Gearing-wise, Favco continues to be in net cash position as at end-September 2018 with a solid war chest of RM330.4 mln, translating to a net cash/share of RM1.49. Net assets/share, meanwhile, stood at RM3.01. No dividends for the quarter were declared as Favco traditionally rewards shareholders with dividends in the final quarter of its financial year-end.

	Y-o-Y			Year-to-date		
	3QFY18	3QFY17	% Chg	9MFY18	9MFY17	% Chg
Revenue						
Local	51.4	52.8	-3%	114.8	128.3	-11%
Overseas	87.2	115.4	-24%	215.9	305.2	-29%
Group	138.6	168.2	-18%	330.7	433.5	-24%

- The reported 9MFY18 net profit amounted to 82.7% of our previous FY18 estimates of RM51.8 mln. As mentioned, the better-than-expected bottom-line was mainly due to the higher contribution from Exact Group. We reckon that the earnings recovery trend shall sustain moving forward in the next few quarters, backed by full-year consolidation of 70%-stake of the four engineering companies – Exact Group – that was acquired on 3rd Jul 2018, coupled with higher recognition from the improving outstanding orderbook. Already, we are seeing an additional 25.2% or RM10.3 mln of pre-tax profit from the aforementioned entities 3QFY18.
- With the reported earnings coming above our expectations, we raised our earnings forecast by 23.2% and 21.2% to RM63.8 mln and RM68.9 mln for FY18 and FY19 respectively. We opine that the global crude oil prices will remain volatile, affected by the softening demand and persistent global supply glut. Nevertheless, we believe Favco is well-positioned to overcome the prevailing slowdown in economic activity over the near term, supported by its healthy balance sheet and relatively sound outstanding orderbook. Going forward, Favco's outstanding orderbook of approximately RM515.0 mln (up from RM427.0 mln in 2QFY18) will provide earnings visibility over the next two years.

Recommendation

Following the recent weakness on its share price, coupled with our earnings revision, we upgraded our recommendation on Favco to **Buy**. Our fair value, however, is unchanged at **RM2.80**, as we peg our revised FY19 profit forecast against a lower target PER of 9.0x (from 10.5x). The lower target PER reflects the general decline in market valuation of mid-small cap stocks listed on Bursa Malaysia along with weak investor sentiment. We nonetheless continue to like Favco for i) its position as a niche integrated crane specialist; ii) established worldwide presence with five manufacturing facilities across the globe; iii) revival of oil & gas works; as well as iv) its sturdy balance sheet with net cash position. Current prospective FY19 valuation of 7.2x PER appears to be undemanding, in our view, with a decent expected dividend yield of approximately 4.4% and 4.9% for FY18 and FY19 respectively.

Key Financials

(FYE Dec)	FY16A	FY17A	FY18F	FY19F
Revenue (RM m)	582.3	526.5	456.6	487.9
<i>Revenue growth</i>	-26.5%	-9.6%	-13.3%	6.9%
EBITDA (RM m)	97.6	98.8	114.8	126.5
Net profit (RM m)	74.6	63.1	63.8	68.9
<i>Net profit growth</i>	-21.2%	-15.5%	1.1%	8.0%
<i>Net profit margin</i>	12.8%	12.0%	14.0%	14.1%
EPS (sen)	33.7	28.5	28.8	31.1
Div/ share (sen)	15.0	13.5	10.0	11.0
Payout ratio	44.5%	47.4%	34.7%	35.3%
BV/share (RM)	2.67	2.84	3.14	3.83
Cash flow/ share (sen)	78.3	53.2	54.8	74.6

Key Valuation Metrics	FY16A	FY17A	FY18F	FY19F
P/E (x)	6.7	7.9	7.8	7.2
P/BV (x)	0.8	0.8	0.7	0.6
P/cashflow (x)	2.9	4.2	4.1	3.0
Dividend yield	6.7%	6.0%	4.4%	4.9%
ROE	12.6%	10.0%	9.2%	8.1%
Net gearing (x)	Net cash	Net cash	Net cash	Net cash

Favco's last 12-month share price chart



Source: Bursa Marketplace

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RATING GUIDE

BUY	Price appreciation expected to exceed 15% within the next 12 months
SELL	Price depreciation expected to exceed 15% within the next 12 months
HOLD	Price movement expected to be between -15% and +15% over the next 12 months from current level

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