# Tenaga Nasional Berhad

***Maintain* BUY**

(5347 | TNB MK) Utilities | Power Generation

## Navigating Extraordinary Times

***Revised* Target Price: RM13.70**

*(from RM13.80 previously)*

### KEY INVESTMENT HIGHLIGHTS

- **1Q20 in line with ours but below consensus**
- **Core earnings lower year-on-year dragged by exceptionally higher provisions given pandemic impact on consumers**
- **Proposing a "gap-year" between RP2 and RP3**
- **Earnings tweaked slightly for stimulus contribution and conservatively assume no clawback of extraordinary provisions**
- **Maintain BUY, TP revised a tad lower to RM13.70 (from RM13.80); significant share price retracement presents value, coupled with reasonably attractive yields**

**Broadly in-line with our expectation.** Tenaga reported a core net profit of RM1.1b (normalized for unrealized forex translation loss of RM388m) for its 1Q20. This is broadly in-line with our estimates but slightly below consensus at 21% and 19% of FY20F respectively. The results also included an exceptionally high provision for doubtful debt of RM99m.

**'Unrealized' forex loss.** The RM388m unrealized forex translation loss (vs. 1Q19 translation gain of RM264m) arises from the volatility of the Ringgit during the early part of the Covid19 outbreak and relates mainly to Tenaga's USD debt. These are however, long-dated debt and has no impact on Tenaga's immediate cash flows. USD debt makes up ~17% of Tenaga's debt portfolio and overall foreign debt makes up ~24% (inclusive of JPY and GBP debt).

**Higher provision for doubtful debt.** 1Q20 core earnings were down -15%yoy given exceptionally high provision for doubtful debt of RM99m in 1Q20. This was taken as a prudent measure in view of the Covid19 pandemic's potential impact on Tenaga's customers. While allowance for doubtful debt (ADD) is provided for as part of Tenaga's regulated cost, the amount is capped based on the pre-agreed RP2 parameters, and is smaller relative to the actual amount that had to be taken given the extraordinary circumstances we are in currently. Nonetheless, Tenaga is understood to be in negotiations with the Energy Commission (EC) to renegotiate the levels of ADD allowable and for a clawback of the exceptionally high amount this year via regulatory adjustments.

**Gap-year proposed.** Tenaga is also proposing to the EC to have one "gap-year" between RP2 (which is ending Dec2020) and RP3 (which is supposed to commence from Jan2021). This is in order to get a better handle of the actual demand and fuel cost trends in setting RP3 parameters, and considering the "out of the ordinary" situation currently caused by the pandemic. Too much deviation against regulatory period parameters would cause a lot of fluctuation in ICPT movements. The "gap-year" is likely to continue on with RP2 parameters while regulated capex might incorporate some that has been planned for RP3.

| RETURN STATISTICS | |
|---|---|
| Price @ 10th June 2020 (RM) | 11.96 |
| Expected share price return (%) | +14.6 |
| Expected dividend yield (%) | +3.8 |
| **Expected total return (%)** | **+18.4** |

**SHARE PRICE CHART**

| Share price performance (%) | Absolute | Relative |
|---|---|---|
| 1 month | -3.1 | -15.0 |
| 3 months | -0.5 | -9.4 |
| 12 months | -0.1 | 4.7 |

| KEY STATISTICS | |
|---|---|
| FBM KLCI | 1,575.27 |
| Syariah compliant | Yes |
| Issue shares (m) | 5686.89 |
| Estimated free float (%) | 31.17 |
| Market Capitalisation (RM'm) | 68,226.98 |
| 52-wk price range | RM10.3 - RM13.6 |
| Beta vs FBM KLCI (x) | 1.00 |
| Monthly velocity (%) | 0.00 |
| Monthly volatility (%) | 11.10 |
| 3-mth average daily volume (m) | 7.24 |
| 3-mth average daily value (RM'm) | 86.19 |
| Top Shareholders (%) | |
| Khazanah Nasional Bhd | 25.69 |
| Employees Provident Fund Board | 16.87 |
| Amanah Saham Nasional Bhd | 12.64 |

**Analyst(s)**
**HAFRIZ** Hezry
hafriz.hezry @midf.com.my
03-2173 8392

## INVESTMENT STATISTICS

| FYE Dec ** | FY17* | FY18 | FY19 | FY20F | FY21F |
|---|---|---|---|---|---|
| Revenue (RM'm) | 63,244.0 | 50,392.5 | 50,939.7 | 54,507.6 | 57,964.4 |
| EBIT (RM'm) | 12,512.6 | 6,887.1 | 8,206.8 | 8,057.7 | 8,327.8 |
| Pre-tax Profit (RM'm) | 10,945.1 | 5,439.7 | 5,277.1 | 6,592.4 | 6,872.5 |
| Core net profit (RM'm) | 10,128.8 | 5,887.3 | 4,721.9 | 4,964.1 | 5,176.9 |
| FD EPS (sen) | 179.5 | 104.3 | 83.7 | 88.0 | 91.7 |
| EPS growth (%) | 30.6 | (41.9) | (19.8) | 5.1 | 4.3 |
| PER (x) | 6.7 | 11.5 | 14.3 | 13.6 | 13.0 |
| Net Dividend (sen) | 82.4 | 53.3 | 100.0 | 44.0 | 45.9 |
| Net Dividend Yield (%) | 6.9 | 4.5 | 8.4 | 3.7 | 3.8 |

*Source: Company, MIDFR   *16-mth period due to change in FY   **FYE Aug prior to FY17*

**Demand trend.** Management guided for a 7%-15% drop in demand this year; the higher end of the range assumes that we are hit by a second wave of the pandemic. In 1Q20, demand contracted -2%yoy (-3%qoq), but 2Q20 should see a more significant impact. Nonetheless, regardless of demand fluctuation, Tenaga's regulated earnings is pretty much defensive as it operates on a revenue-cap basis under the IBR with the exception of the retail segment (on price-cap basis) which accounts for 0.6% of regulated earnings. Tenaga's regulated earnings is essentially compensated for a shortfall in demand (vs. the 1.8%-2.0% annual demand growth projected under RP2). Vice versa, Tenaga has to return excess earnings if demand exceeds the RP2 projections. For the most part of RP2 however, demand had exceeded forecasts and Tenaga and been returning the excess earnings. The generation segment meanwhile, is governed by PPAs and attains capacity payment based on plant availability to the grid.

**Earnings revision.** Though the 1Q20 results were within our expectation, we tweak our FY20F/21F by 3%/1% to factor in: (1) The RM150m CSR contribution by Tenaga towards electricity rebates which came as part of the stimulus package announced by the Government earlier, running between April 2020 till September 2020. The bulk of the electricity rebates however, will be funded by the Government and the EIF (Electricity Industry Fund), and the impact is limited to FY20F. (2) We conservatively factor in higher provision for doubtful debt given uncertainties arising from the pandemic on the end-consumers; despite Tenaga's effort to clawback the amount via negotiations with the EC, we conservatively assume no clawback is achieved in our projections for the meantime. Our forecasts are 4.6%/4.7% below consensus over FY20F/21F.

**Recommendation.** Maintain **BUY** on Tenaga. Our DCF-based **TP** is revised a tad lower to **RM13.70** (from RM13.80 previously) given the tweaks to our earnings in this report. Tenaga's share price has retraced significantly in the past month and we see value emerging while dividend yields are reasonably attractive. This is underpinned by: (1) Easing capex for generation in the near-to-mid-term, which suggests base dividends of at least at the higher end of the group's 30%-60% payout policy (2) Stretched Government fiscal position suggests potentially higher cash upflow requirement from key GLCs.

## TENAGA NASIONAL: 1QFY20 RESULTS SUMMARY

| FYE Dec (RMm) | 1Q19 | 4Q19 | 1Q20 | YoY | QoQ |
|---|---|---|---|---|---|
| Revenue | 13,245 | 12,177 | 11,655 | -12.0% | -4.3% |
| **EBITDA** | **4,963** | **4,115** | **4,814** | **-3.0%** | **17.0%** |
| Depreciation | (2,457) | (2,765) | (2,590) | 5.4% | -6.3% |
| EBIT | 2,506 | 1,350 | 2,224 | -11.3% | 64.8% |
| Net interest expense | (576) | (834) | (794) | 37.9% | -4.7% |
| Forex translation gain/(loss) | 264 | 277 | (388) | | |
| Associates/JVs | (6) | (59) | 16 | 357.4% | 126.5% |
| FV change of financial instruments | (58) | 47 | (26) | | |
| Pretax profit (before forex translation) | 1,810 | 498 | 1,404 | -22.4% | 181.9% |
| Tax | (552) | (191) | (280) | -49.4% | 46.7% |
| Minority Interest | (36) | (69) | 19 | -152.8% | -127.2% |
| Reported net profit | 1,557 | 653 | 718 | -53.9% | 9.9% |
| **Core net profit** | **1,293** | **477** | **1,106** | **-14.5%** | **132.0%** |
| Reported EPS (sen) | 27.4 | 11.5 | 12.6 | -53.9% | 9.9% |
| **Core EPS (sen)** | **22.8** | **8.4** | **19.5** | **-14.5%** | **132.0%** |
| | | | | | |
| DPS (sen) | - | 70.00 | - | NA | NA |
| | | | | | |
| EBITDA margin | 37.5% | 33.8% | 41.3% | | |
| EBIT margin | 18.9% | 11.1% | 19.1% | | |
| Pretax margin (pre-forex transation) | 13.7% | 4.1% | 12.1% | | |
| Tax rate | -30.5% | -38.3% | -19.9% | | |
| Core net profit margin | 9.8% | 3.9% | 9.5% | | |
| Payout ratio | 0.0% | 608.4% | 0.0% | | |

*Source: Company, MIDFR*

## TENAGA NASIONAL: 1QFY20 RESULTS BREAKDOWN

| Unit Revenue/Cost Analysis | 1Q19 | 4Q19 | 1Q20 | YoY | QoQ |
|---|---|---|---|---|---|
| **Average tariff achieved for TNB sale (sen/kwH)** | **39.80** | **39.80** | **41.08** | **3.2%** | **3.2%** |
| *Sales-to-Generation* | *90.5%* | *90.7%* | *87.6%* | | |
| **Demand sales volume (GWh)** | **28,471** | **28,774** | **27,938** | **-1.9%** | **-2.9%** |
| Generation volume (GWh) | 31,444 | 31,719 | 31,908 | 1.5% | 0.6% |
| Unit Revenue (RM/kwh) | 0.3980 | 0.3980 | 0.4108 | 3.2% | 3.2% |
| | | | | | |
| **Unit Cost (RM/kwH) - Total cost** | **0.375** | **0.392** | **0.342** | **-8.9%** | **-13.0%** |
| Unit Cost (RM/kwH) - IPP & TNB Fuels | 0.176 | 0.160 | 0.141 | -20.1% | -11.9% |
| | | | | | |
| Unit Cost (RM/kwH) - Repair & maintenance | 0.015 | 0.022 | 0.016 | 7.9% | -27.7% |
| Unit Cost (RM/kwH) - General expenses | 0.016 | 0.026 | 0.014 | -12.5% | -48.0% |
| Unit Cost (RM/kwH) - Staff cost | 0.023 | 0.032 | 0.028 | 20.8% | -12.3% |
| | | | | | |
| **Gross Electricity Sale Revenue (RMm):** | **11,912.8** | **12,087.3** | **12,021.9** | **0.9%** | **-0.5%** |
| TNB (without ICPT) | 11,331.3 | 11,453.4 | 11,477.7 | 1.3% | 0.2% |
| EGAT | 0.1 | - | 0.1 | NA | NA |
| SESB | 461.8 | 474.2 | 467.5 | 1.2% | -1.4% |
| LPL | 88.3 | 130.7 | 43.1 | -51.2% | -67.0% |
| Tenaga Wind Ventures | 31.3 | 29.0 | 33.5 | 7.0% | 15.5% |
| | | | | | |

*Source: Company, MIDFR*

## TENAGA NASIONAL: 1QFY20 GENERATION MIX

| Generation Mix (Includes IPPs) | 1Q19 (%) | 4Q19 (%) | 1Q20 (%) | Variance (%) YoY |
|---|---|---|---|---|
| Gas & LNG | 41.9 | 41.5 | 30.5 | (11.4) |
| Coal | 54.6 | 53.1 | 64.6 | 10.0 |
| Distillate | 0.1 | 0.0 | 0.0 | (0.1) |
| Oil | 0.1 | 0.2 | 0.0 | (0.1) |
| Hydro | 2.9 | 4.6 | 4.2 | 1.3 |
| Solar | 0.4 | 0.6 | 0.7 | 0.3 |
| **Fuel Cost Composition** | **1Q19 (%)** | **4Q19 (%)** | **1Q20 (%)** | **Variance (%) YoY** |
| Gas & LNG | 49.0 | 55.7 | 42.3 | (6.7) |
| Coal | 49.9 | 43.4 | 57.3 | 7.4 |
| Distillate | 0.3 | 0.3 | 0.2 | (0.0) |
| Oil | 0.2 | 0.5 | 0.2 | (0.0) |
| Solar | 0.7 | 0.0 | 0.0 | (0.7) |

*Source: Company, MIDFR*

## TENAGA NASIONAL: 1QFY20 COST ANALYSIS

| Cost Analysis (RMm) | 1Q19 | 4Q19 | 1Q20 | YoY | QoQ |
|---|---|---|---|---|---|
| IPP purchase cost | 3,581.0 | 3,237.5 | 2,420.0 | -32.4% | -25.3% |
| *- Capacity payment* | *59.4* | *46.7* | *21.6* | -63.6% | -53.7% |
| *- Energy payment* | *3,521.6* | *3,190.8* | *2,398.4* | -31.9% | -24.8% |
| Fuel costs | 2,511.3 | 2,606.6 | 2,599.7 | 3.5% | -0.3% |
| Repair & Maintenance | 460.7 | 693.1 | 504.4 | 9.5% | -27.2% |
| Staff cost | 729.2 | 1,012.7 | 893.9 | 22.6% | -11.7% |
| TNB General Expenses | 494.7 | 839.1 | 439.0 | -11.3% | -47.7% |
| Subsi. COS & Opex | 446.3 | 139.4 | 97.6 | -78.1% | -30.0% |
| Depreciation & Amortisation | 2,457.5 | 2,764.7 | 2,590.0 | 5.4% | -6.3% |
| Net loss on impairment of financial instrument | - | - | - | NA | NA |
| **Total** | **10,680.7** | **11,293.1** | **9,544.6** | **-10.6%** | **-15.5%** |

*Source: Company, MIDFR*

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# DISCLOSURES AND DISCLAIMER



| MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS | |
|---|---|
| **STOCK RECOMMENDATIONS** | |
| **BUY** | Total return is expected to be >10% over the next 12 months. |
| **TRADING BUY** | Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow. |
| **NEUTRAL** | Total return is expected to be between -10% and +10% over the next 12 months. |
| **SELL** | Total return is expected to be <10% over the next 12 months. |
| **TRADING SELL** | Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow. |
| **SECTOR RECOMMENDATIONS** | |
| **POSITIVE** | The sector is expected to outperform the overall market over the next 12 months. |
| **NEUTRAL** | The sector is to perform in line with the overall market over the next 12 months. |
| **NEGATIVE** | The sector is expected to underperform the overall market over the next 12 months. |