

28 May 2018 | 1QFY18 Results Review

Tenaga Nasional

Time to bottom fish?

- **1Q18 earnings in-line, seasonally strong margins**
- **Sufficient EIF to cover surcharge, uncertain about rebates**
- **Stock has taken quite a beating, value emerging**
- **TP unchanged at RM16.30 but stock upgraded to BUY**

Earnings in-line. Tenaga reported 1Q18 core earnings of RM2b This is within expectations accounting for 27% of both our and consensus' FY18F respectively. This is the first FYE Dec quarterly reporting hence no yoy or qoq comparison was available.

Margins frontloaded. Operational cost and capex are seasonally lower at the start of the year, hence EBITDA margins were pretty strong at 34.4% in 1Q18. We see this normalising to a range of 30%-33% in the coming quarters.

Strong volume growth. 1Q18 volume growth of 2.3%yoy was in line with recent years' trend. Demand from the industrial segment was particularly strong at +4.4%yoy in line with the country's manufacturing performance. However unlike RP1, RP2 entails a revenue cap mechanism eliminating volume/effective rate excesses or underperformance against RP2 parameters. At this point however, adjustments have yet to be made as the revised regulatory guidelines and mechanism for this have yet to be finalised.

Sufficient buffer for 2H18. Besides opex savings in RP1 and PPA savings, the EIF (Electricity Industry Fund) also entails financial savings from underspent capex (RM1.5b variance against forecast capex) in RP1. The EIF fund is estimated to amount to RM1.5b. The 1H18 is expected to utilise RM929m to subsidise an ICPT surcharge of 0.28sen and a 1.52sen rebate. While the EIF is sufficient to cover an ICPT surcharge for 2H18, it is uncertain if the amount is sufficient to maintain the 1.52sen rebate (estimated at RM785m). Elimination of the rebate could raise effective tariff by 4%.

A dilemma. While we acknowledge that the new Government aims to be business friendly (hence IBR is likely to remain intact), at the same time, policies so far have been populist. It is uncertain if the new Government is willing to bite the bullet to raise tariffs less than a year of taking office. To strike a balance (in the case the current EIF is run down) we think the Government might assume the role of subsidising consumers (via its own contribution to the EIF fund perhaps), much the same way petrol is (planned to be) subsidised and similar to Government compensation to toll operators in the past if a scheduled rate hike is delayed.

Upgraded BUY
Unchanged Target Price: RM16.30

RETURN STATS	
Price (25 May 2018)	RM15.04
Target Price	RM16.30
Expected Share Price Return	+8.4%
Expected Dividend Yield	+4.8%
Expected Total Return	+13.2%

STOCK INFO	
KLCI	1,797.40
Bursa / Bloomberg	5347/TNB MK
Board / Sector	Main
Syariah Compliant	Yes
Issued shares (mil)	5678.18
Market cap. (RM'm)	85,399.84
Price over NA	1.50
52-wk price Range	RM13.7 - RM16.3
Beta (against KLCI)	0.68
3-mth Avg Daily Vol	11m
3-mth Avg Daily Value	RM174m
Major Shareholders (%)	
Khazanah Nasional	28.1%
EPF	12.4%
Skim ASB	8.3%

INVESTMENT STATISTICS

FYE Dec **	FY15	FY16	16MFY17*	FY18F	FY19F
Revenue (RM'm)	43,286.8	44,531.5	63,244.0	50,573.5	53,266.0
EBIT (RM'm)	7,695.3	9,072.0	12,512.6	9,160.5	9,710.9
Pre-tax Profit (RM'm)	7,133.7	8,456.8	10,945.1	8,290.5	8,454.8
Core net profit (RM'm)	5,978.9	7,757.6	10,128.8	7,373.8	6,379.5
FD EPS (sen)	105.9	137.5	179.5	130.7	113.0
EPS growth (%)	27.7	29.7	30.6	(27.2)	(13.5)
PER (x)	14.2	10.9	8.4	11.5	13.3
Net Dividend (sen)	29.0	32.0	82.4	71.9	62.2
Net Dividend Yield (%)	1.9	2.1	5.5	4.8	4.1
Payout ratio	26.7%	24.5%	48.1%	55.0%	55.0%

* 16-month period due to change in financial year end from Aug to Dec

** FYE Aug prior to FY17

Source: Company, MIDF

Time to bottom fish? Tenaga's share price has been bashed down quite substantially, presumably given the perceived risk on its ability to attain a tariff hike, and secondly, given Tenaga's reasonably high foreign shareholding (of 24%) among index stocks. Given substantial price depreciation in the past week, we now see value emerging. Our TP remains unchanged at RM16.30, but we raise our call to BUY from NEUTRAL. Dividend yields are now attractive at 4.8% (+ve spread against 10yr MGS of 4.26%) while valuations are cheap at 12x FY18F earnings, a substantial discount to the market's 16x-17x.

EXHIBIT 1: TENAGA 1Q18 RESULT

Financial Year End 31 Dec (RMm, unless otherwise stated)	1QFY18
Revenue	12,274.0
EBITDA	4,221.7
Depreciation	(1,532.0)
EBIT	2,689.7
Net interest expense	(280.4)
Translation gain/(loss)	89.0
Associates/JVs	(77.0)
Pretax profit (before forex translation)	2,326.4
Tax	(298.6)
Minority Interest	(2.9)
Reported net profit	2,119.7
Core net profit	1,988.5
Reported EPS (sen)	37.6
Core EPS (sen)	35.2
DPS (sen)	-
EBITDA margin	34.4%
EBIT margin	21.9%
Pretax margin (pre-forex transation)	19.0%
Tax rate	-12.8%
Core net profit margin	16.2%
Payout ratio	0.0%

Source: Company, MIDF

EXHIBIT 2: TENAGA 1Q18 RESULT BREAKDOWN

Unit Revenue/Cost Analysis	1QFY18
Average tariff achieved for TNB sale (sen/kwH)	39.57
Demand sales volume (GWh)	27,070
Unit Revenue (RM/kwh)	0.3957
Unit Cost (RM/kwH) - Total cost	0.361
Unit Cost (RM/kwH) - IPP & TNB Fuels	0.190
Unit Cost (RM/kwH) - Repair & maintenance	0.016
Unit Cost (RM/kwH) - General expenses	0.017
Unit Cost (RM/kwH) - Staff cost	0.035
Gross Electricity Sale Revenue (RMm):	11,281.4
TNB	10,712.5
EGAT	1.3
SESB	543.5
LPL	13.8
Tenaga Wind Ventures	10.3

Source: Company, MIDF

EXHIBIT 3: TENAGA 1Q18 GENERATION MIX

Generation Mix (Includes IPPs)	1QFY18 (%)
Gas & LNG	41.2
Coal	53.8
Distillate	0.0
Oil	0.0
Hydro	4.9
Fuel Cost Composition	1QFY18 (%)
Gas & LNG	46.3
Coal	53.3
Distillate	0.3
Oil	0.2

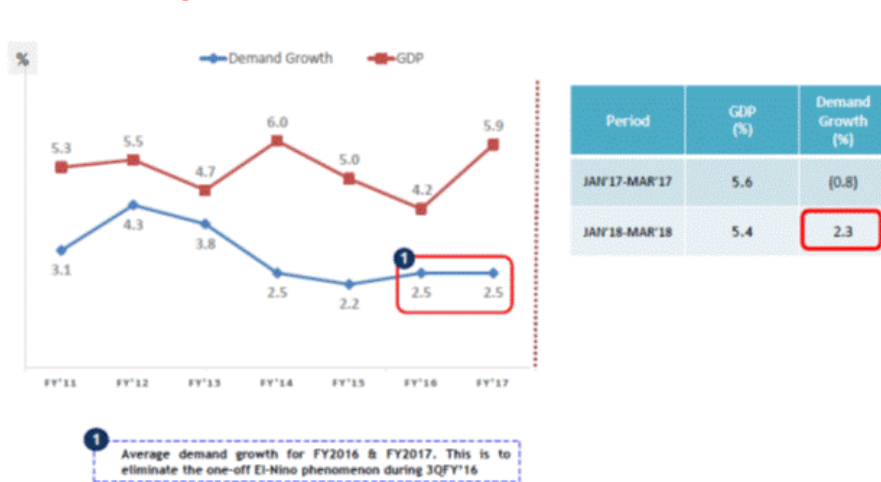
Source: Company, MIDF

EXHIBIT 3: TENAGA 1Q18 COST ANALYSIS

Cost Analysis (RMm)	1QFY18	Composition 1QFY18
IPP purchase cost	3,664.6	38%
- Capacity payment	1,009.1	10%
- Energy payment	2,655.5	27%
Fuel costs	2,482.3	25%
Repair & Maintenance	433.3	4%
Staff cost	939.1	10%
TNB General Expenses	469.9	5%
Subs. COS & Opex	245.6	3%
Depreciation & Amortisation	1,532.0	16%
Total	9,766.8	100%

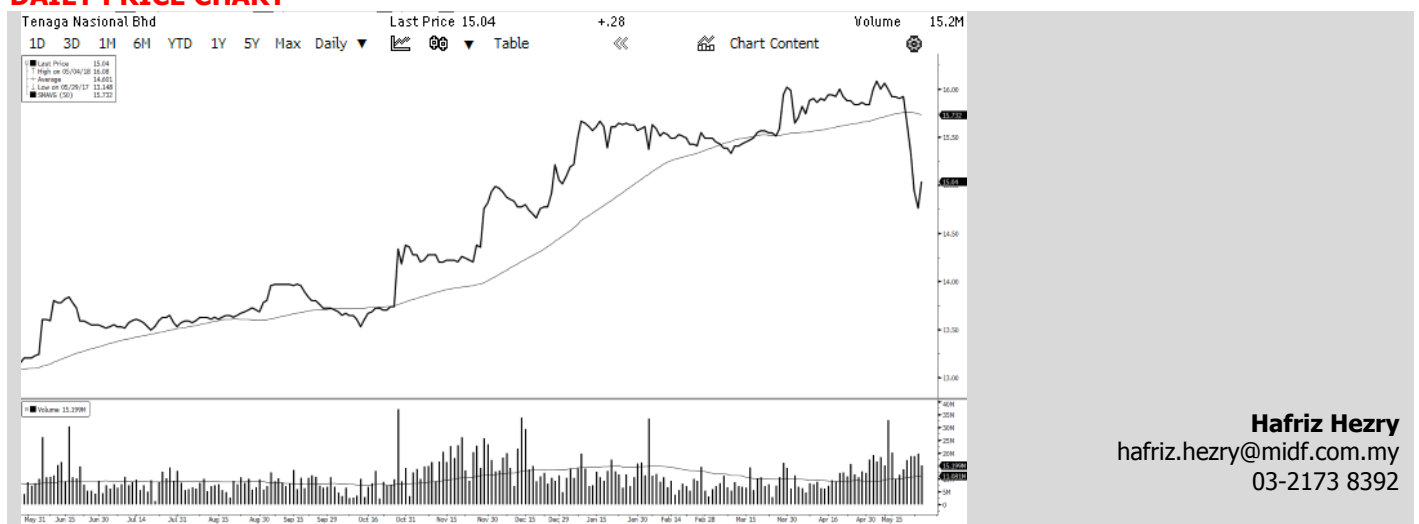
Source: Company, MIDF

EXHIBIT 4: 1Q18 DEMAND GROWTH IN LINE WITH PAST TRENDS



Source: Company, MIDF

DAILY PRICE CHART



Source: Bloomberg, MIDFR

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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 <i>rise</i> 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 <i>fall</i> 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.