Sector Update | Wednesday, 10 May 2023

UTILITIES

***Maintain* NEUTRAL**

Pickings from the Latest ICPT Announcement

KEY INVESTMENT HIGHLIGHTS

- **Latest ICPT review reflects easing fuel cost**
- **Water and sewerage operators are the biggest winners given sharp reduction in ICPT surcharge**
- **Solar EPCC players stand to benefit from relaxed conditions for Net Energy Metering and Self-Consumption programs**
- **Our sector picks are YTL Power (BUY, TP: RM1.54), YTL Corp (BUY, TP: RM1.05) and Ranhill Utilities (BUY, TP: RM0.73)**

Latest ICPT reflects easing fuel cost. The latest 2H23 ICPT review reflects easing global fuel prices, in particular, coal price which has more than halved peak levels of USD463/MT seen in 2H22. However, the Government's targeted subsidy rollback continues, with high consumption domestic consumers now charged a 10sen/kwh surcharge from a -2sen/kwh rebate previously. In the non-domestic consumer segment, a clear winner are the water and sewerage utilities (now under a new category), which are now charged a much lower 3.7sen/kwh surcharge from a 20sen/kwh surcharge previously. All in, the Government will still bear a subsidy of RM5.2b, albeit less than half of the RM10.8b subsidy allocated for the 1H23 period. Summary of the latest ICPT decision:

(1) Domestic consumers with <1500kwh/month consumption will continue to enjoy the current -2sen/kwh rebate, while **domestic consumers with >1500kwh/month consumption are now charged a 10sen/kwh surcharge**.

(2) **ICPT surcharge for medium and high voltage non-domestic consumers is reduced to 17sen/kwh** from 20sen/kwh, resulting in a 5% reduction in effective tariffs. Meanwhile low voltage non-domestic consumers (<11kv connection) as well as those in the agriculture sector will continue to pay a 3.7sen/kwh surcharge.

(3) **Water and sewerage operators are now under a special category**, which will see their ICPT surcharge reduce to 3.7sen/kwh from 20sen/kwh previously.

Easing working capital for Tenaga. Although coal price has come off significantly, market price at the latest USD133/MT are still 68% higher than RP3 projection of USD79/MT. Additionally, the Ringgit continues to remain weak at USD:RM4.6, weaker than RP3 projection of USD:RM4.12. As such, we expect **Tenaga**'s **(NEUTRAL, TP: RM10.00)** ICPT under-recovery position to remain in the near-term, albeit at much lower levels than that in 2H22. Easing under-recovery is expected to drive lower working capital requirement, ease Tenaga's receivables and allow it to retire some of its previous short-term financing positions. However, the positives from improved cash flows are already reflected in our valuation.

COMPANY IN FOCUS

Ranhill Utilities Bhd
Maintain **BUY** | Unchanged Target price: RM0.73
Price @ 23rd June 2023: RM0.52

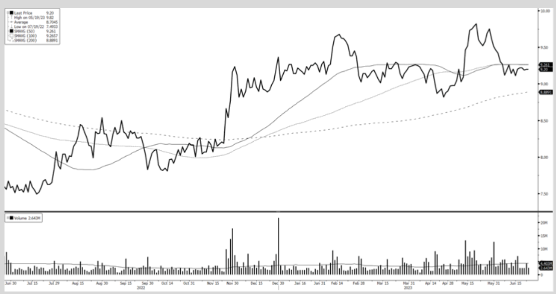
- Biggest winner of latest ICPT review from large reduction in surcharge
- Benefitting from non-domestic water tariff hike since Jan23'
- Upcoming domestic water tariff review a potential catalyst

Share price chart

Tenaga Nasional Bhd
Maintain **NEUTRAL** | Unchanged Target price: RM10.00
Price @ 23rd June 2023: RM9.20

- Easing cash flow pressure from peaking receivables and working capital requirement
- Earnings neutral to ICPT decision

Share price chart



ANALYST:
Hafriz Hezry
hafriz.hezry@midf.com.my
03 -2173 8392

Water utilities are the biggest winners. The new segmentation for water and sewerage operators was a pleasant surprise as it were previously categorised as mid-to-high voltage consumers (>11kv connection) which were charged the highest range ICPT surcharge of 20sen/kwh. The new 3.7sen/kwh surcharge is a significant reduction, translating into a -27% reduction in effective tariffs to 43.65sen/kwh (inclusive of 39.95sen/kwh base tariff). We believe **Ranhill Utilities**' **(BUY, TP: RM0.73)** strong 1QFY23 earnings momentum could gain further traction in 2HFY23 with this latest announcement. Pending further checks with management, we see potential +26%/+29% upside to Ranhill's FY23F/24F earnings from lower electricity cost.

Table 1: Summary of 2H23 ICPT Review

	2H23 ICPT Review (sen/kwh)					
	Domestic		Non-domestic			
	<1500KWh/mth consumption	>1500KWh/mth consumption	<11kv connection	>11kv connection	Water/sewerage utilities*	Agriculture
Base tariff	39.95	39.95	39.95	39.95	39.95	39.95
ICPT surcharge/(rebate)	(2.00)	10.00	3.70	17.00	3.70	3.70
Effective tariff	**37.95**	**49.95**	**43.65**	**56.95**	**43.65**	**43.65**
Change from 1H23	*0.0%*	*31.6%*	*0.0%*	*-5.0%*	*-27.2%*	*0.0%*

Source: NRECC, MIDFR **previously categorised as >11kv non-domestic*

	1H23 ICPT (sen/kwh)			
	Domestic	Non-domestic		
		<11kv connection	>11kv connection	Agriculture
Base tariff	39.95	39.95	39.95	39.95
ICPT surcharge/(rebate)	(2.00)	3.70	20.00	3.70
Effective tariff	**37.95**	**43.65**	**59.95**	**43.65**

Source: NRECC, MIDFR

Catalyst for RE sector. The Government is relaxing conditions for the Net Energy Metering (NEM) and self-consumption (SELCO) for solar PV programs (effective 15th July) by: (1) Increasing allowable capacity to 85% of consumption from 75% previously for both NEM and SELCO, (2) Allowing participation of high voltage consumers in the SELCO program. We believe these will encourage further solar PV adoption by both domestic and non-domestic consumers, while the latter should complement the existing NEM program without impacting the grid's solar penetration limit (SELCO programs are non-grid connected, unlike NEM). Additionally, we believe the increase in effective tariffs for high-consumption domestic consumers will encourage adoption of rooftop solar to reduce electricity cost.

Recommendation. The latest ICPT announcement is broadly positive for mid-to-high voltage non-domestic consumers (industrial and commercial sectors) given a -5% reduction in effective electricity cost, while the biggest winner is the water and sewerage sector given a significant -27% reduction in effective tariffs. While we remain **NEUTRAL**, we see selective opportunities within the utilities sector; we believe power utilities players operating in liberalised electricity markets (rather than regulated ones) are better positioned to benefit from improved demand-supply conditions and can more efficiently manage higher input cost - **YTL Power (BUY, TP: RM1.54)** and **YTL Corp (BUY, TP: RM1.05)** are plays into this given exposure to the Singapore power sector. While we note the recent announcement by the Energy Market Authority of the temporary switch to a dynamic price cap, we believe this would have limited impact on YTL Power as the majority of YTL Power's capacity is locked in long-term contracts. Additionally, it is one of the more efficient generators - capping price spikes is likely to affect generators with the least efficient capacity as they are the last to get on the grid, in our opinion. We also like the water utilities space as a play into the recent non-domestic sector tariff hike and the upcoming domestic sector tariff review; our pick in the water utilities sector is **Ranhill Utilities (BUY, TP: RM0.73)**. **Tenaga (NEUTRAL, TP: RM10.00)** is earnings neutral to the ICPT decision, but the Government's commitment to the ICPT mechanism and the reduction in under-recovery from easing fuel cost underpins improvements in its receivables position leading to improved cash flow prospects. However, the positives from these are already reflected in our valuation. Meanwhile, solar EPCC players such as **Solarvest**, **Samaiden**, **Sunview** and **Pekat** stand to benefit from the relaxed conditions for NEM and SELCO.

Chart 1: Newcastle coal price

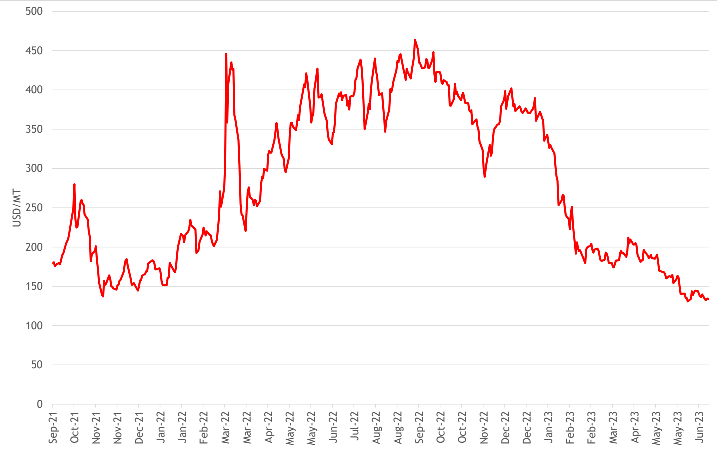
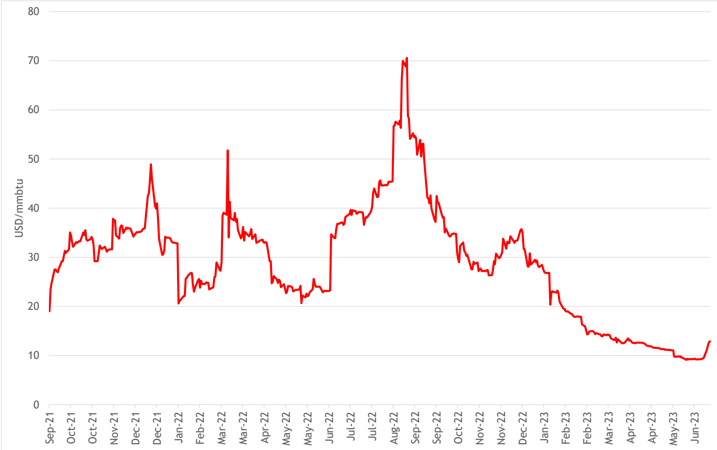


Chart 2: LNG Price (Japan Korea marker)



Source: Bloomberg, MIDFR

Chart 3: Tenaga's average coal price delivered

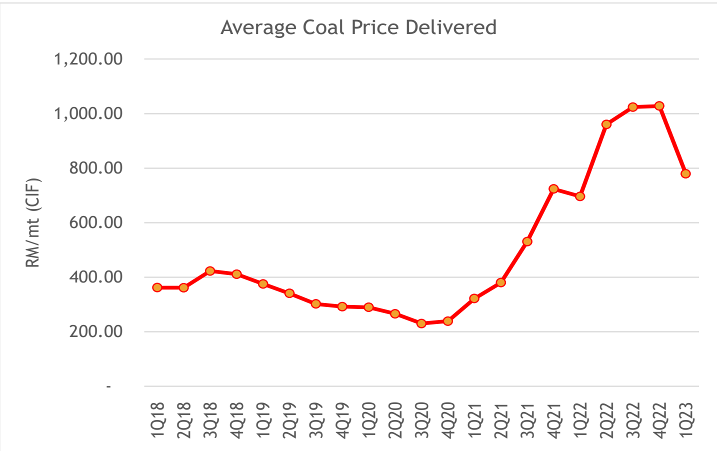
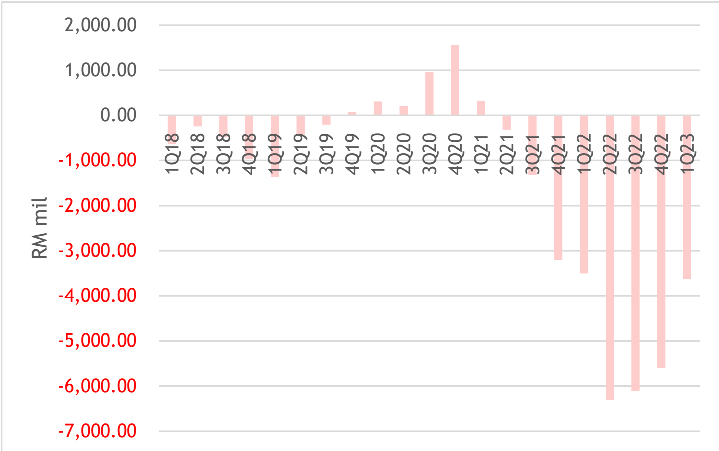
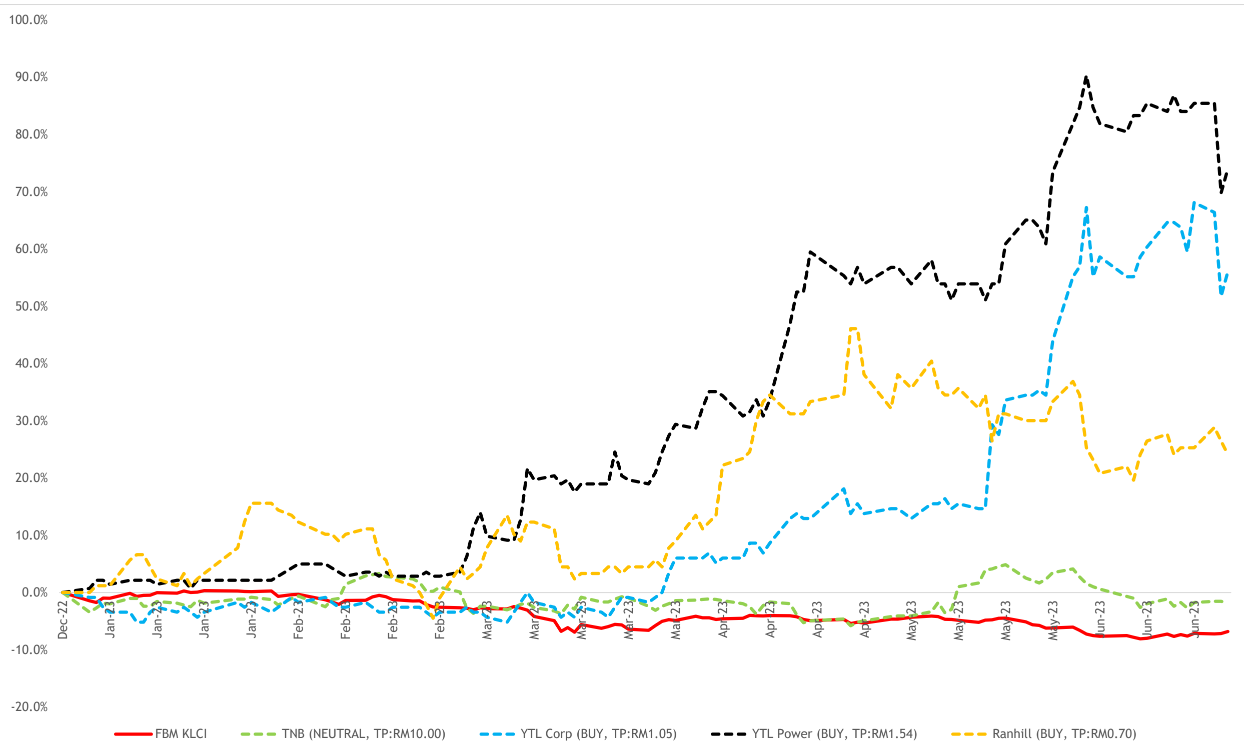


Chart 4: Tenaga's ICPT over/(under) recovery



Source: Tenaga, MIDFR

Chart 5: Share price performance of utilities stocks under our coverage vs. the FBM KLCI



Source: Bloomberg, MIDFR

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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology