

Tenaga Nasional (TNB MK)

Renewables push continues

RE progress marred by ICPT concerns

Tenaga closed its first RE deal of 2022, thus making further progress with its renewable push (8,300MW by 2025). Nevertheless, soaring coal prices means concerns over the ICPT mechanism will continue to take centre stage. Maintain HOLD with an unchanged MYR9.30 TP (DCF-based). We prefer Mega First (MFCB MK, BUY, CP: MYR3.71, TP: MYR4.30) and YTL Power (YTLP MK, BUY, CP: MYR0.675, TP: MYR0.90) in the Utilities space.

Acquiring UK onshore wind farms

Tenaga via Vantage (its wholly-owned UK RE subsidiary) has acquired 97.3MW of UK onshore wind farms for GBP145.9m (c.MYR805m), from funds advised by Capital Dynamics, an independent asset management firm. Details are limited. The acquired portfolio comprises of 11 UK sites developed under either the Feed-in Tariff or Renewable Obligation Certificate subsidy regimes, thus providing some degree of revenue stability. The acquisition raises Vantage's wind capacity from 433MW to 530MW, and Tenaga's gross RE capacity from 3,479MW to 3,576MW.

Coal prices continue to climb

Based on latest operating logs, 1Q22 Peninsular Malaysia generation was up c.1.8% YoY and down c.2.4% QoQ. In our view, generation is back at the pre-pandemic run-rate. Meanwhile, coal prices have continued to climb, with the Newcastle spot averaging 35% higher QoQ in 1Q22. The under-recovery of Tenaga's generation costs will thus continue. With the Industry Fund likely close to depleted, the government's options to avoid fully passing-through a surcharge are increasingly limited.

Maintain HOLD

Our earnings forecasts and MYR9.30 TP (DCF-based assuming 8.4% WACC and 1% LT growth) are unchanged. While valuations are attractive and ESG concerns seemingly largely priced-in, we think the stock is unlikely to re-rate significantly in the near term due to lingering concerns over the ICPT mechanism.

FYE Dec (MYR m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	43,976	52,630	48,844	49,677	50,525
EBITDA	13,860	15,326	15,430	15,725	16,077
Core net profit	4,459	5,141	4,660	5,021	5,205
Core FDEPS (sen)	77.9	89.5	81.1	87.4	90.6
Core FDEPS growth(%)	(12.7)	14.8	(9.4)	7.7	3.7
Net DPS (sen)	80.0	40.0	36.6	39.5	40.9
Core FD P/E (x)	13.4	10.4	11.2	10.4	10.0
P/BV (x)	1.1	0.9	0.9	0.8	0.8
Net dividend yield (%)	7.7	4.3	4.0	4.4	4.5
ROAE (%)	7.4	7.6	8.0	8.3	8.2
ROAA (%)	2.5	2.8	2.5	2.7	2.7
EV/EBITDA (x)	7.0	6.4	6.2	6.0	5.8
Net gearing (%) (incl perps)	62.7	72.7	68.1	62.6	57.1
Consensus net profit	-	-	4,647	5,021	5,205
MKE vs. Consensus (%)	-	-	0.3	(0.0)	0.0

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HOLD

Share Price MYR 9.07
12m Price Target MYR 9.30 (+7%)
Previous Price Target MYR 9.30

Company Description

Tenaga Nasional engages in the generation, transmission, distribution and sale of electricity and the provision of other related services.

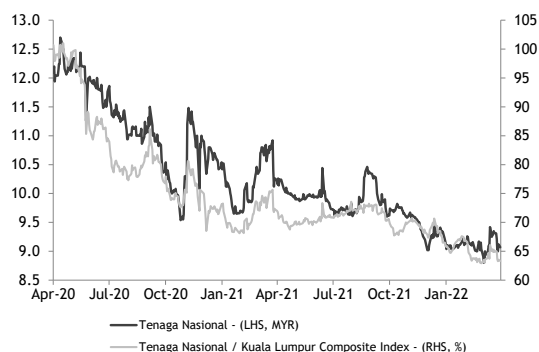
Statistics

52w high/low (MYR)	10.46/8.80
3m avg turnover (USDm)	10.4
Free float (%)	55.6
Issued shares (m)	5,705
Market capitalisation	MYR51.7B USD12.3B

Major shareholders:

Khazanah Nasional Bhd	25.6%
Employees Provident Fund	15.9%
Permodalan Nasional Bhd	9.7%

Price Performance



	-1M	-3M	-12M
Absolute (%)	0	(1)	(12)
Relative to index (%)	0	(5)	(13)

Source: FactSet

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Risk Rating & Score ¹	38.0 (High)
Score Momentum ²	+2.1
Last Updated	19 Nov 2021
Controversy Score ³ (Updated: 3 Dec 2021)	1 - Customer (quality & safety) incidents

Business Model & Industry Issues

- With the commissioning of Jimah East, Malaysia’s diversification into coal plants over the past decade has ended. New plants going forward will be gas or solar-based. The unit cost of generation for both gas and solar plants are for now still higher than coal, although this is essentially borne by consumers via the IBR tariff framework.
- Given the prevailing structure of PPAs in Malaysia, coal will however continue to feature very prominently in Peninsular Malaysia’s generation mix for at least the next decade. This means the “coal stigma” will continue to accompany Tenaga for the foreseeable future. Should such pressure increase, Tenaga could consider accelerating its renewable expansion (it already has international solar and wind platforms) or potentially de-merging or spinning off its generation unit.
- The push into renewables has seen the increased adoption of solar via solar farms and rooftop solar. From a land optimisation perspective, the technology is probably better suited for rooftops. With the right incentives, Tenaga’s panel leasing business could become more significant in contribution.

Material E issues

- Significant coal exposure with coal accounting for over 50% of Peninsular Malaysia’s generation mix. However, many of these coal plants are new and utilises ultra-supercritical technology. Meanwhile, the cost of insuring coal plants has risen by 10-20% annually in recent years.
- Balance of generation is largely gas-based, which is still a fossil fuel and thus create carbon emissions. In response, Tenaga has in recent years, been consciously increasing its renewable capacity in line with the government’s target of achieving a 20% renewable mix by 2025.
- Large-scale renewable facilities such as solar farms and hydro dams are typically land-intensive (a 50MW farm requires c.200 acres of land) and could have an effect on local biodiversity. In Peninsular Malaysia, there are no longer suitable sites for large dams while solar farms are typically situated on unused agricultural land.

Material S issues

- Average electricity tariffs in 2020 are c.20% higher relative to 2013 levels, steep for an essential service. Nevertheless, households have largely been insulated, with tariffs for the two lowest bands (c.70% of households) having been kept unchanged for the past decade.
- Tenaga was found liable for causing flash floods at Cameron Highlands (Bertam Valley) in 2013 having discharged water from its hydroelectric dam following heavy rains. Tenaga has since proactively engaged preventive measures such as regular cleaning of reservoir and dam, and conducting annual flood evacuation drills.
- Tenaga is a major employer in Malaysia, with a staff count of about 35,000 people of which 23,000 are represented by unions. 21% of Tenaga’s employees are female. It also owns and operates a leading university in Malaysia which enrolls c.10,000 students.

Key G metrics and issues

- Tenaga’s constitution states a minimum of 2 and a maximum of 12 directors. MoF Inc being the special shareholder of Tenaga, has the right to appoint up to six directors.
- There are presently 11 members on Tenaga’s board comprising of 1 Executive Director (President/CEO), 3 Non-Independent Non-Executive Directors (including the Chairman) and 7 Independent Non-Executive Directors.
- 3 of the 11 board members (including Chairman and President/CEO are appointees by MoF Inc and Khazanah Nasional.
- In terms of board gender and diversity, 3 of the 11 board members are female, 3 are non-bumiputeras and 7 are of non-finance/accounting backgrounds.
- Tenaga has been audited by PricewaterhouseCoopers for at least the past decade.
- The cumulative remuneration of the 6 highest-paid top executives represents less than 0.3% of Tenaga’s 2020 normalised net profit.
- Female representation at the management level remains relatively low at 22% among senior management and 7% among top management.
- Tenaga’s track record with its international acquisitions has been mixed - it has substantially impaired its associates in Turkey (fully written-off) and India a few years after acquisition.
- Tenaga’s balance sheet remains relatively under-levered, with a net debt-to-equity of just 65% at end 2020. MFRS 16 with its lease liabilities has inflated the reported net gearing to c.1.1x, still a comfortable level.

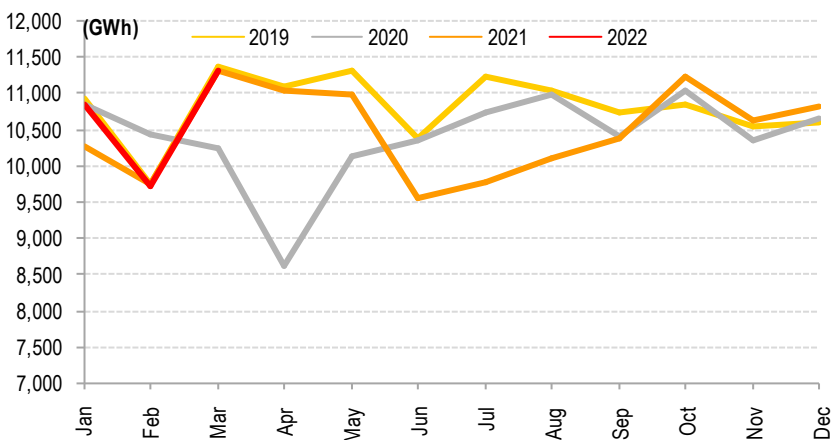
¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company’s exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company’s enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company’s score since the last update - a **negative** integer indicates a company’s improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Capital Dynamics pre-transaction UK onshore wind portfolio

Site	MW	Status	Location
Whiteside Hill	13.5	Operational	Scotland
Dunmore	21	Operational	Ireland
Airfield	8.6	Operational	England
Middle Balbeggie	6.4	Operational	Scotland
Potato Pot	7.1	Operational	England
Wythegill	1.5	Operational	Workington
Seegronan	6.9	Operational	Northern Ireland
Shantavny		Operational	Northern Ireland
Crockandun	7.5	Operational	Northern Ireland
Elginny		Operational	Northern Ireland
Tod Hill	11.4	Operational	Scotland
Harthill	5.7	Operational	Scotland
Ysgellog	4.6	Operational	Wales
Garlenick	4	Operational	Cornwall
Daintree	4	Operational	Northamptonshire
East Youlstone	4	Operational	Devon
Mossmorran	4.6	Operational	Scotland
Red Gap	12.5	Operational	England
Westnewton	6.2	Operational	England
Watford Lodge	10.3	Operational	England
Antrim	11.5	Operational	Northern Ireland
Tyrone	8.1	Operational	Northern Ireland
Castlegore	23.1	Pre-Construction	Northern Ireland
Longhill	50	Pre-Construction	Scotland
Sorbie	12.6	Pre-Construction	Scotland
Total	245.1		

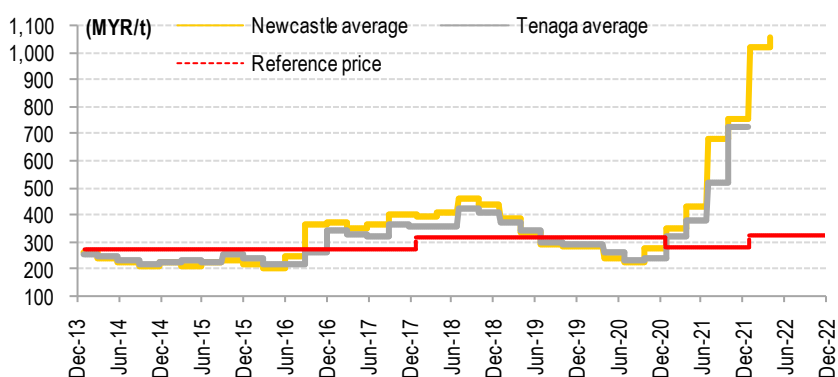
Source: Capital Dynamics

Pen Msia monthly electricity generation



Source: Energy Commission

Coal prices



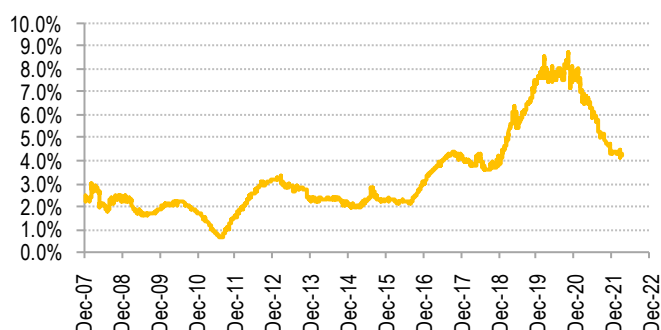
Source: Bloomberg, Maybank IBG research

Trailing PER



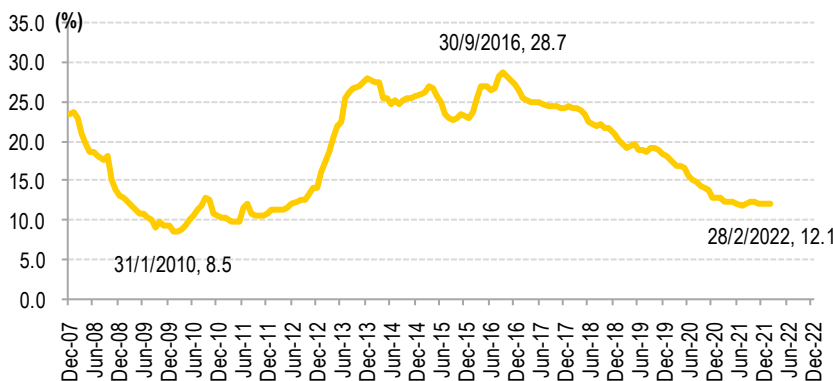
Source: Bloomberg, Maybank IBG research

Trailing net yield



Source: Bloomberg, Maybank IBG research

Foreign shareholding



Source: Company

Risk statement

There are several risk factors for our earnings estimates, price target, and rating for Tenaga. Regulatory developments, such as the determination of regulated returns, have direct impact on earnings. Changes in electricity demand patterns or plant outages could also result in loss of earnings for Tenaga.

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Key Metrics					
P/E (reported) (x)	15.6	13.2	11.1	10.3	10.0
Core P/E (x)	13.3	10.4	11.1	10.3	10.0
Core FD P/E (x)	13.4	10.4	11.2	10.4	10.0
P/BV (x)	1.1	0.9	0.9	0.8	0.8
P/NTA (x)	2.9	2.5	2.2	1.9	1.8
Net dividend yield (%)	7.7	4.3	4.0	4.4	4.5
FCF yield (%)	14.5	9.2	9.8	11.4	12.2
EV/EBITDA (x)	7.0	6.4	6.2	6.0	5.8
EV/EBIT (x)	14.2	12.0	11.7	11.3	10.8
INCOME STATEMENT (MYR m)					
Revenue	43,976.0	52,629.5	48,843.9	49,676.9	50,524.9
EBITDA	13,859.6	15,326.4	15,430.2	15,725.2	16,077.2
Depreciation	(7,021.2)	(7,218.1)	(7,302.8)	(7,411.4)	(7,513.1)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	6,838.4	8,108.3	8,127.5	8,313.8	8,564.1
Net interest income / (exp)	(1,638.2)	(1,909.6)	(2,141.4)	(2,179.6)	(2,205.1)
Associates & JV	76.5	193.5	193.5	193.5	193.5
Exceptionals	(253.0)	(858.0)	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	5,023.7	5,534.2	6,179.6	6,327.7	6,552.5
Income tax	(793.9)	(1,048.7)	(1,316.9)	(1,104.2)	(1,144.6)
Minorities	(23.7)	(202.9)	(202.9)	(202.9)	(202.9)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	4,206.1	4,282.6	4,659.8	5,020.7	5,205.0
Core net profit	4,459.1	5,140.6	4,659.8	5,020.7	5,205.0
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	13,415.4	9,208.4	12,304.7	16,037.6	20,062.7
Accounts receivable	10,216.8	13,976.9	13,381.9	13,065.7	13,150.3
Inventory	1,583.8	1,977.1	1,830.9	1,859.3	1,885.6
Property, Plant & Equip (net)	113,213.1	114,105.6	115,802.8	117,391.5	118,378.4
Intangible assets	35,340.3	35,149.6	35,149.6	35,149.6	35,149.6
Investment in Associates & JVs	1,339.2	1,867.1	1,995.6	2,124.1	2,252.6
Other assets	6,324.7	6,315.9	6,315.9	6,315.9	6,315.9
Total assets	181,433.3	182,600.6	186,781.4	191,943.7	197,195.2
ST interest bearing debt	6,409.1	6,992.5	6,992.5	6,992.5	6,992.5
Accounts payable	10,534.1	8,596.7	7,832.1	7,850.5	7,856.8
LT interest bearing debt	43,043.5	44,685.7	46,911.3	49,136.9	51,362.5
Other liabilities	63,997.0	63,933.0	63,933.0	63,933.0	63,933.0
Total Liabilities	123,983.4	124,208.2	125,669.2	127,913.2	130,145.1
Shareholders Equity	55,833.2	56,608.4	59,171.3	61,932.6	64,795.4
Minority Interest	1,616.7	1,784.0	1,940.9	2,097.8	2,254.7
Total shareholder equity	57,449.9	58,392.4	61,112.2	64,030.4	67,050.1
Total liabilities and equity	181,433.3	182,600.6	186,781.4	191,943.7	197,195.2
CASH FLOW (MYR m)					
Pretax profit	5,023.7	5,534.2	6,179.6	6,327.7	6,552.5
Depreciation & amortisation	7,021.2	7,218.1	7,302.8	7,411.4	7,513.1
Change in working capital	(1,006.9)	(5,798.0)	(23.4)	306.1	(104.6)
Other operating cash flow	5,685.5	5,233.7	(193.5)	(193.5)	(193.5)
Cash flow from operations	15,518.6	13,353.9	14,089.9	14,927.2	14,827.9
Capex	(6,909.7)	(8,415.5)	(9,000.0)	(9,000.0)	(8,500.0)
Free cash flow	8,608.9	4,938.4	5,089.9	5,927.2	6,327.9
Dividends paid	(5,235.8)	(4,568.4)	(2,096.9)	(2,259.3)	(2,342.3)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	2,004.5	1,886.0	2,225.6	2,225.6	2,225.6
Other invest/financing cash flow	(2,795.2)	(1,688.1)	(2,122.4)	(2,160.6)	(2,186.1)
Effect of exch rate changes	0.0	0.0	0.0	0.0	0.0
Net cash flow	2,582.4	567.9	3,096.3	3,732.9	4,025.2

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Key Ratios					
Growth ratios (%)					
Revenue growth	(13.7)	19.7	(7.2)	1.7	1.7
EBITDA growth	(4.0)	10.6	0.7	1.9	2.2
EBIT growth	(8.5)	18.6	0.2	2.3	3.0
Pretax growth	(14.1)	10.2	11.7	2.4	3.6
Reported net profit growth	(14.2)	1.8	8.8	7.7	3.7
Core net profit growth	(12.2)	15.3	(9.4)	7.7	3.7
Profitability ratios (%)					
EBITDA margin	31.5	29.1	31.6	31.7	31.8
EBIT margin	15.6	15.4	16.6	16.7	17.0
Pretax profit margin	11.4	10.5	12.7	12.7	13.0
Payout ratio	108.4	53.4	45.0	45.0	45.0
DuPont analysis					
Net profit margin (%)	9.6	8.1	9.5	10.1	10.3
Revenue/Assets (x)	0.2	0.3	0.3	0.3	0.3
Assets/Equity (x)	3.2	3.2	3.2	3.1	3.0
ROAE (%)	7.4	7.6	8.0	8.3	8.2
ROAA (%)	2.5	2.8	2.5	2.7	2.7
Liquidity & Efficiency					
Cash conversion cycle	(12.9)	13.5	39.6	38.6	37.1
Days receivable outstanding	76.0	82.7	100.8	95.8	93.4
Days inventory outstanding	19.1	15.8	18.5	17.6	17.6
Days payables outstanding	108.0	85.1	79.7	74.9	73.9
Dividend cover (x)	0.9	1.9	2.2	2.2	2.2
Current ratio (x)	0.9	1.0	1.1	1.2	1.4
Leverage & Expense Analysis					
Asset/Liability (x)	1.5	1.5	1.5	1.5	1.5
Net gearing (%) (incl perps)	62.7	72.7	68.1	62.6	57.1
Net gearing (%) (excl. perps)	62.7	72.7	68.1	62.6	57.1
Net interest cover (x)	4.2	4.2	3.8	3.8	3.9
Debt/EBITDA (x)	3.6	3.4	3.5	3.6	3.6
Capex/revenue (%)	15.7	16.0	18.4	18.1	16.8
Net debt/ (net cash)	36,037.2	42,469.8	41,599.1	40,091.8	38,292.3

Source: Company; Maybank IBG Research

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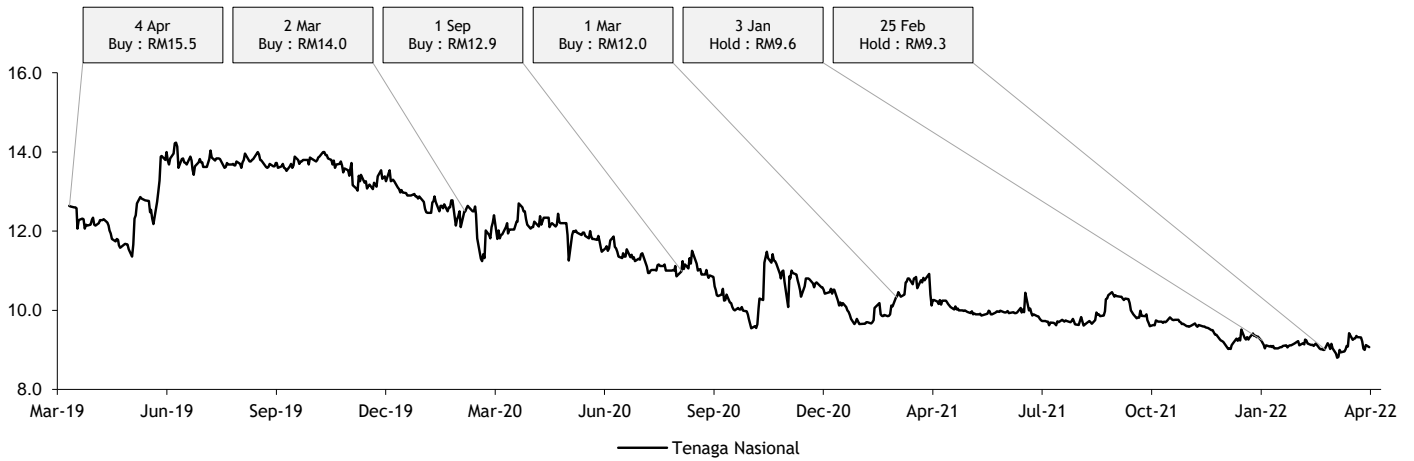
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