

Tenaga Nasional

Getting Ready For Market Reform

By Teh Kian Yeong | tehky@kenanga.com.my

TENAGA has revealed an internal restructuring to split power generation and retail businesses into RetailCo and GenCo that will have their own board and management teams. This is to pave the way for the impending market reform. We maintain that the fears of open competition is overplayed given that RetailCo would only contribute <3% to group earnings. Until market could accept that such risk is manageable, MP is the best call for TENAGA currently.

Internal reorganisation in place. On Monday, TENAGA announced a proposed internal reorganisation which will see two new wholly-owned subsidiaries set up to house the domestic power generation business (GenCo) and the electricity retail business (RetailCo) while the structure for the remaining businesses such as transmission and distribution network, international business and corporate centre remains unchanged at the group level. These two new entities shall have their own separate board and management teams. This reorganisation is expected to be completed by 3Q20. In all, it is to prepare for the upcoming reforms in the electricity supply industry with the Energy Minister expecting to reveal the Malaysia Electricity Supply Industry (MESI) 2.0 next month.

Two new entities to prepare for the reform. As the retail business is highly anticipated to open up for new comers, RetailCo is prepared to improve efficiency to increase customer collection rate, which is currently slightly <1 sen/kWh and at the same time it will involve rooftop solar generation as well as pushing beyond energy offerings such as multi-utility bundling and billing, Fibre-to-the-Home broadband, or sales of 3rd parties' products. Meanwhile, besides conventional capacity, GenCo is aiming to improve RE generation through participation in Large-Scale Solar (LSS) scheme. In addition, GenCo will continue to go for offshore expansion for its O&M business under REMACO. For assets size indication, the pro-forma FY18 book value for RetailCo was c.RM1.84b against the group's book value of RM59.05b while GenCo has a book value of RM12.14b.

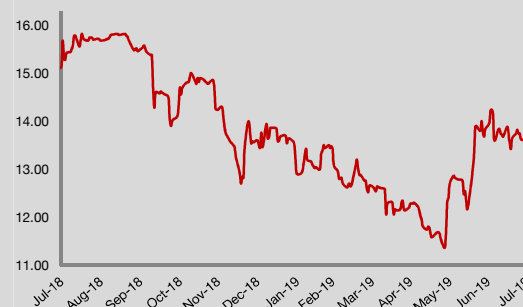
Group earnings to double by 2025. Contributions from these two entities are fairly small for the moment, with RetailCo's EBIT of RM0.2b only making up <3% of Group FY18 EBIT of RM6.7b while GenCo's RM1.6b accounted for 5.4% of group earnings. As such, the fears of opening up retail business are seen as overly played. TENAGA is aimed to target EBIT of RM13.0b by 2025 with RetailCo earnings growing to RM0.7b with GenCo earnings to increase to RM2.6b. Given the regulated IBR framework, this aim is a tall order which means it has to grow its non-RAB business tremendously especially the international business in order to double its earnings. This is despite that fact that TENAGA may lose out some earnings for RetailCo and eventually GenCo as well if this segment is opened up.

More clarity but MP for now. There is higher clarify now pertaining to RetailCo earnings, but we believe the market may need time to digest while waiting for the announcement of MESI 2.0. Thus, we maintain our MARKET PERFORM rating with an unchanged target price of RM13.40, which is based on 13.6x FY20 PER, in-line with 1SD-band below its 2-year mean. Our recommendation is supported by 3-4% yield. Overall, this restructuring is paving the way for the market reform and the impending new structure could lead to two separate listing entities under two segments. Risks to our recommendation are: (i) the stronger-than-expected earnings from non-regulated business as well as (ii) a higher dividend payout.

MARKET PERFORM ↔

Price : **RM13.62**
Target Price : **RM13.40** ↔

Share Price Performance



KLCI 1,642.69
YTD KLCI chg -2.8%
YTD stock price chg 0.1%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TNB MK
Market Cap (RM m)	77,455.4
Shares outstanding	5,686.9
52-week range (H)	16.00
52-week range (L)	11.24
3-mth avg daily vol:	6,262,502
Free Float	43%
Beta	1.3

Major Shareholders

Khazanah Nasional Bhd	27.3%
Employees Provident Fund	15.3%
State Street Corp	14.1%

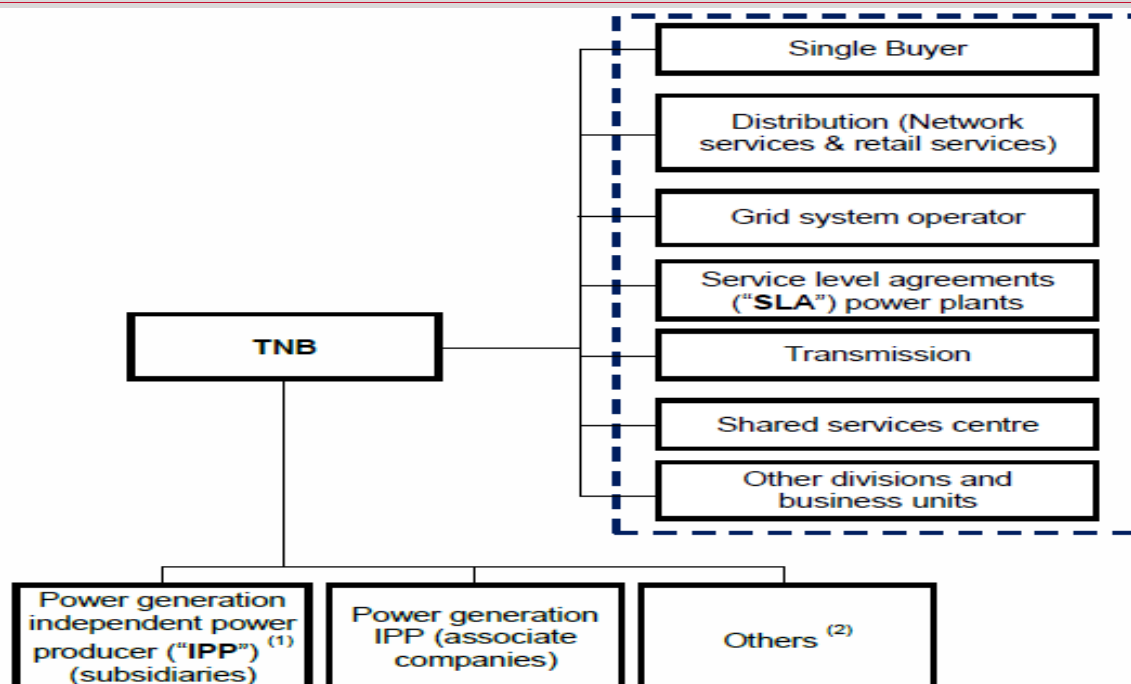
Summary Earnings Table

FYE Dec (RM m)	2018	2019E	2020E
Turnover	50,393	52,017	52,960
EBIT	8,271	9,106	9,001
PBT	5,046	7,367	7,515
Net Profit (NP)	3,724	5,559	5,672
Core Net Profit	5,470	5,559	5,672
Consensus (NP)		5,572	5,749
Earnings Revision (%)		-	-
Core EPS (sen)	96.3	97.9	99.9
EPS growth (%)	-10.4	1.6	2.0
NDPS (sen)	53.3	49.0	49.9
BV/Share (RM)	10.2	10.7	11.2
NTA/Share (RM)	10.1	10.6	11.1
Core PER (x)	14.1	13.9	13.6
PBV (x)	1.3	1.3	1.2
Price/NTA (x)	1.3	1.3	1.2
Net Gearing (x)	0.51	0.46	0.44
Net Yield (%)	3.9	3.6	3.7



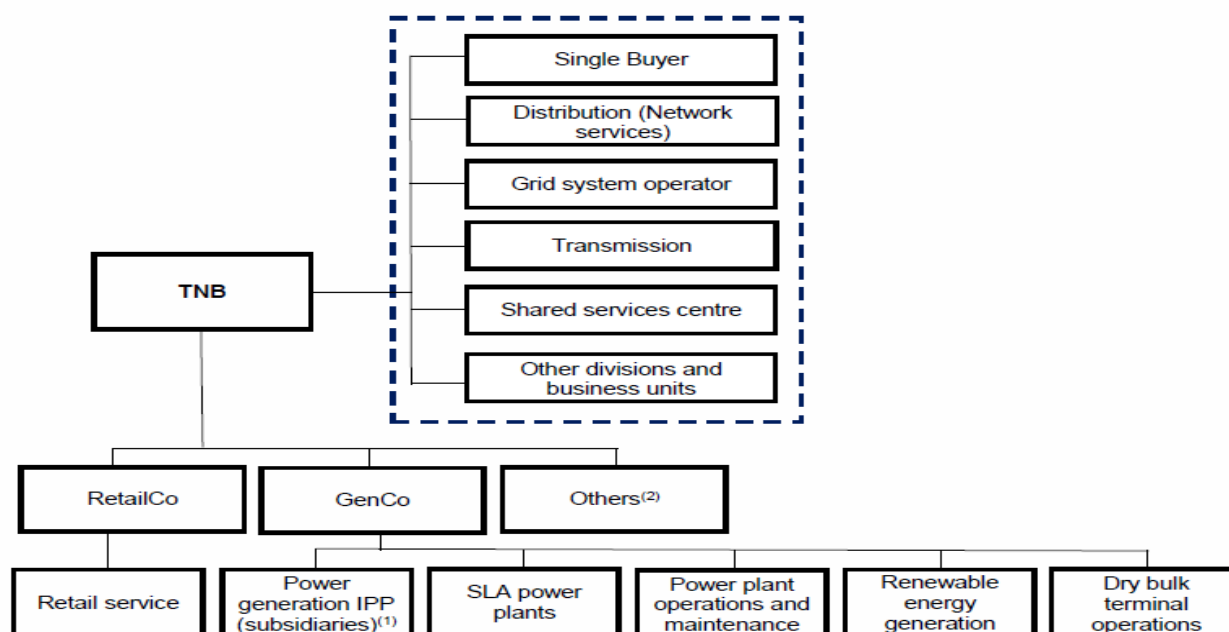
31 July 2019

Before The Proposed Internal Reorganisation



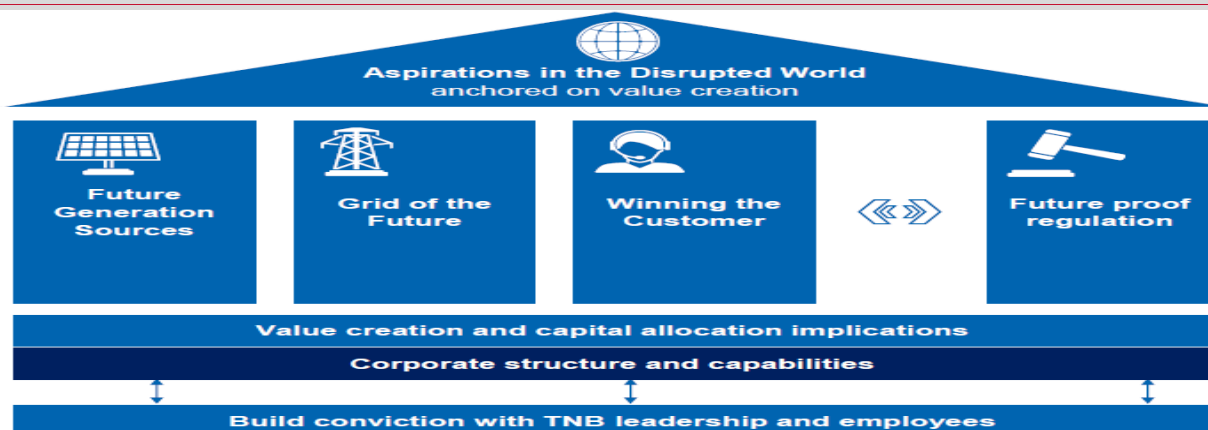
Note: (1) inclusive of local and international IPPs; (2) Other subsidiaries and associate companies
Source: Company

After The Proposed Internal Reorganisation



Note: (1) Excluding the Excluded Power Plants, which shall remain in TENAGA; (2) Other subsidiaries, associate companies and business units including power generation IPP (associate companies) and Excluded Power Plants.
Source: Company

TENAGA's Strategic Aspiration - A Key Enabler Is The Corporate Structure



Source: Company

Internal Reorganisation Is Focused On Generation & Retail Corporatisation



Source: Company

Rationale For Internal Reorganisation

Value and focus



- Focus on efficiency, agility and performance
- GenCo and RetailCo with separate boards and management
- Flexibility in capital management

Transparency



- Clarity on business performance of each value chain segment
- Separation of regulated and major non-regulated businesses

Preparedness for disruption

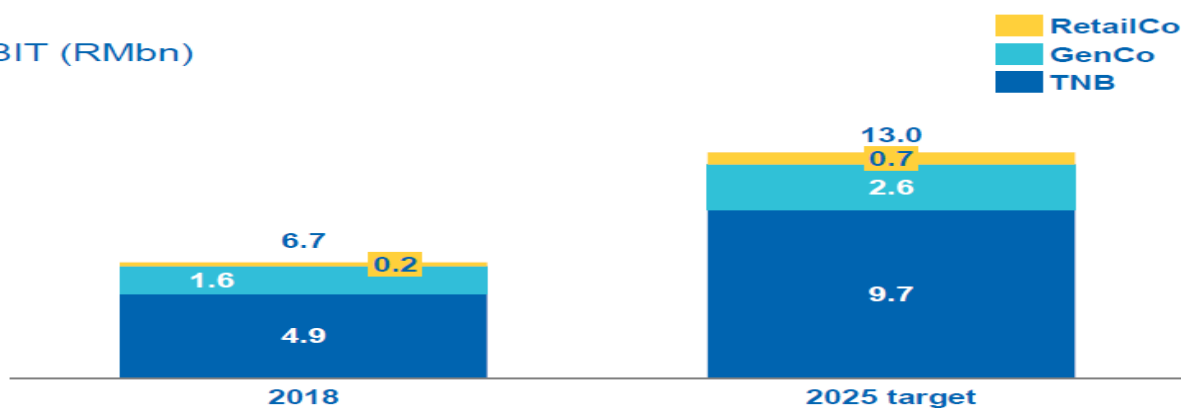


- Adapt to expected changes to the electricity supply industry
- Prepare for increased competition
- Pursue new growth opportunities

Source: Company

TENAGA Is Targeting RM13b EBIT In 2025

EBIT (RMbn)



Source: Company

GenCo: Realise Synergies From E2E Capabilities To Capture Domestic Growth

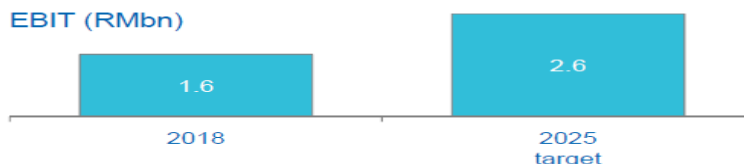
Market context

- Lower near term demand growth with PPAs expiring
- Potential higher growth conventional and in RE in the medium term
- Potential changes in market structure

Outlook for GenCo

- Realise synergies and efficiencies of end-to-end power generation
- Capture opportunities in RE and medium term conventional prospects

EBIT (RMbn)



Growth

- Increase conventional capacity through plant-ups and repowering projects
- Increase RE generation through continued participation in the Large Scale Solar (LSS) scheme
- Continue international expansion of REMACO

Efficiency

- Leverage synergies through procurement and generation excellence

Source: Company

TENAGA: National Network Operator, Strategic Guide & International Growth Driver

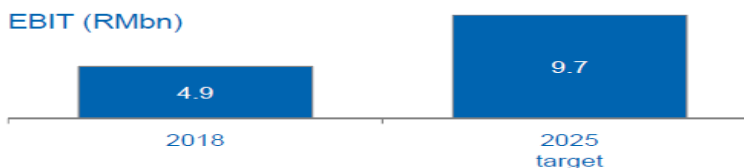
Context

- Expectations for network to support distributed generation, energy efficiency and electric vehicle aspirations
- International opportunities across power value chain

Outlook for TNB

- Sustain and enhance the national grid
- Focus first on turnaround of international assets; take a more hands-on role in overseas ventures

EBIT (RMbn)



Growth

- Investment into smart grid, supporting distributed generation and variable loads
- Turnaround and strengthen existing international assets ahead of growth through more activist participation
- Continue to identify growth opportunities in the utilities sector

Efficiency

- Optimize network through procurement excellence, and operations & maintenance best practices
- Streamline corporate costs

Source: Company

31 July 2019

RetailCo: Retailer Of Choice With Leading Green & Energy Service Portfolios

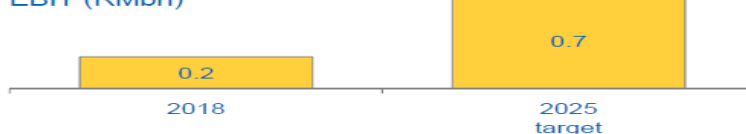
Context

- Potential market liberalization and competition
- Higher customer expectations with anticipated choice
- Increasing government support for green prosumers

Outlook for RetailCo

- Win the customer with enhanced customer service and offerings
- Serve emerging green retail market

EBIT (RMbn)



Growth

- Lead rooftop solar generation by leveraging TNB's scale and RetailCos customer relationships
- Push out beyond meter products such as smart solutions for homes and businesses, battery storage, or energy trading platforms
- Push out beyond energy offerings such as multi-utility bundling and billing, Fibre-To-The-Home (FTTH) broadband, or sales of third-party products

Efficiency

- Improve cost-competitiveness of the solar rooftop business through efficient procurement and financing strategies
- Increase customer collection rates even further from today

Source: Company

Internal Reorganisation Targets 3Q20 completion



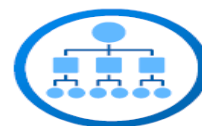
Today - Bursa Announcement

Approval of proposed internal reorganisation



H1 2020 - Court process

Legal process to transfer assets & liabilities through Scheme of Arrangement



Q3 2020 - New corporate structure

New corporate structure in place

Source: Company

The Internal Reorganisation Is Subject To A numbers Of Approvals Being Obtained

- Approval of the **shareholders of TNB at a court-convened meeting** to be convened for the Proposed Internal Reorganisation
- Order of the **High Court sanctioning the Scheme and granting of the Vesting Orders** in relation to the Proposed Internal Reorganisation
- Approval/consents of the **financiers/creditors of TNB**
- Approval/consents of **MESTECC, EC and MOF**
- Approval, consent and/or sanction of **any other relevant authorities/parties** (e.g. State Land Authorities), if required

Source: Company

31 July 2019

Income Statement

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Revenue	47417	15827	50393	52017	52960
EBITDA	15469	5199	14762	15855	16080
Depreciation	-6105	-2050	-6491	-6749	-7079
Operating Profit	9364	3149	8271	9106	9001
Other Income	238	134	424	348	398
Interest Expense	-1456	-576	-1689	-1887	-1683
Associate	128	-37	-189	-200	-200
Excep. Items	0	0	-1354	0	0
PBT	8282	2979	5046	7367	7515
Taxation	-1370	-235	-1301	-1768	-1804
Minority Interest	-8	12	-21	-40	-40
Net Profit	6904	2756	3724	5559	5672
Core Net Profit	6067	2036	5470	5559	5672

Balance Sheet

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Fixed Assets	103084	104808	111446	114696	117617
Intangible Assets	211	211	241	240	240
Other FA	11197	11522	11259	11450	11450
Inventories	829	885	1296	991	1010
Receivables	9104	10510	10381	8733	8891
Other CA	12532	10927	10722	10780	10780
Cash	5056	5415	8370	7423	5902
Total Assets	142012	144277	153714	154313	155891
Payables	11335	10198	10995	11124	11343
ST Borrowings	1808	1745	3928	1846	1820
Other ST Liability	2183	2311	6948	6930	6921
LT Borrowings	37038	39698	43905	43734	41940
Other LT Liability	32063	32195	28886	28808	29138
Minorities Int.	473	925	1214	1253	1276
Net Assets	57111	57205	57838	60617	63453
Share Capital	11125	11200	11446	11446	11446
Reserves	45987	46005	46392	49171	52007
Equity	57111	57205	57838	60617	63453

Cashflow Statement

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Operating CF	11631	1526	11666	15794	13076
Investing CF	-12842	-2008	-10414	-10000	-10000
Financing CF	2295	843	402	-6792	-4596
Change In Cash	1084	361	1655	-998	-1521
Free CF	-1211	-482	1253	5794	3076

Financial Data & Ratios

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Growth					
Turnover (%)	6.5	0.1	6.1	3.2	1.8
EBITDA (%)	4.6	0.8	-5.3	7.4	1.4
Operating Profit (%)	3.2	0.9	-12.4	10.1	-1.2
PBT (%)	2.7	7.9	-43.5	46.0	2.0
Net Profit (%)	-6.3	19.7	-55.0	49.3	2.0
Core Net Profit (%)	-9.3	0.7	-10.4	1.6	2.0
Profitability (%)					
EBITDA Margin	32.6	32.8	29.3	30.5	30.4
Operating Margin	19.7	19.9	16.4	17.5	17.0
PBT Margin	17.5	18.8	10.0	14.2	14.2
Net Margin	14.6	17.4	7.4	10.7	10.7
Core Net Margin	12.8	12.9	10.9	10.7	10.7
Effective Tax Rate	40.9	26.8	23.6	25.8	24.0
ROE	11.1	10.7	9.5	12.8	9.1
ROA	5.5	5.5	4.8	6.4	4.7
DuPont Analysis					
Net Margin (%)	14.6	17.4	7.4	10.7	10.7
Assets Turnover (x)	0.3	0.1	0.3	0.3	0.3
Leverage Factor (x)	2.5	2.5	2.7	2.5	2.5
ROE (%)	12.1	4.8	6.4	9.2	8.9
Leverage					
Debt/Asset (x)	0.3	0.3	0.3	0.3	0.3
Debt/Equity (x)	0.7	0.7	0.8	0.8	0.7
Net Cash/(Debt)	-21568	-25539	-29528	-28158	-27858
Net Debt/Equity (x)	0.38	0.45	0.51	0.46	0.44
Valuations					
EPS (sen)	106.8	35.9	96.3	97.9	99.9
NDPS (sen)	61.0	21.4	53.3	49.0	49.9
BV/share (RM)	10.1	10.1	10.2	10.7	11.2
NTA/share (RM)	10.0	10.0	10.1	10.6	11.1
PER (x)	12.7	12.7	14.1	13.9	13.6
Net Yield (%)	4.5	1.6	3.9	3.6	3.7
P/BV (x)	1.4	1.4	1.3	1.3	1.2
P/NTA (x)	1.4	1.4	1.3	1.3	1.2
EV/EBITDA (x)	6.4	6.5	7.4	6.7	4.8

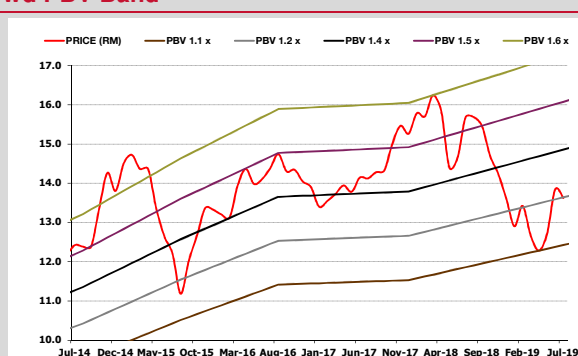
Note: old YE was Aug; New YE is Dec; Dec-17 was from Sep 2017 to Dec 201

Source: Kenanga Research

Fwd PER Band



Fwd PBV Band



Source: Bloomberg, Kenanga Research

31 July 2019

Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target	Rating
	(RM)	Cap	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
GAS MALAYSIA BHD	2.85	3,659.4	Y	12/2019	2.9%	7.7%	8.2%	2.2%	21.5	19.9	19.5	3.6	3.3	17.3%	3.8%	3.05	MP
MALAKOFF CORP BHD	0.905	4,422.7	Y	12/2019	-0.3%	-0.1%	10.5%	4.5%	20.6	18.7	17.9	0.8	0.8	4.3%	4.3%	1.00	OP
PESTECH INTERNATIONAL BHD	1.44	1,100.6	Y	06/2019	6.7%	22.2%	28.0%	30.9%	17.7	13.8	10.6	2.4	2.0	16.0%	0.0%	2.00	OP
PETRONAS GAS BHD	16.18	32,015.9	Y	12/2019	4.8%	-1.8%	5.7%	-14.7%	17.5	16.6	19.5	2.5	2.3	14.5%	4.2%	16.55	MP
TENAGA NASIONAL BHD	13.62	77,455.4	Y	12/2019	3.2%	1.8%	2.6%	2.0%	14.2	13.9	13.6	1.3	1.3	9.3%	3.6%	13.40	MP
YTL POWER INTERNATIONAL BHD	0.795	6,101.9	N	06/2019	3.4%	2.6%	-1.6%	8.0%	9.1	9.3	8.6	0.4	0.4	4.6%	6.3%	0.880	MP
Simple Average					3.4%	5.4%	8.9%	5.5%	16.8	15.3	14.9	1.8	1.7	11.0%	3.7%		

Source: Bloomberg, Kenanga Research

This section is intentionally left blank

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

This document has been prepared for general circulation based on information obtained from sources believed to be reliable but we do not make any representations as to its accuracy or completeness. Any recommendation contained in this document does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may read this document. This document is for the information of addressees only and is not to be taken in substitution for the exercise of judgement by addressees. Kenanga Investment Bank Berhad accepts no liability whatsoever for any direct or consequential loss arising from any use of this document or any solicitations of an offer to buy or sell any securities. Kenanga Investment Bank Berhad and its associates, their directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein from time to time in the open market or otherwise, and may receive brokerage fees or act as principal or agent in dealings with respect to these companies.

Published and printed by:

KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia

Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my

