

04 December 2019

Tenaga Nasional

Tax Dispute Worries Over-rated

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ICPT surcharge is set to be reduced in 1HCY20 given the fall in fuel prices but this is earnings-neutral as the savings will be passed through to consumer with a 6-month lag. A RM4b tax dispute last week resulted in a sell-down which aggravated its already weak share price trend. This could be a good buying opportunity as the market has over-reacted to the tax issue which is a non-operational issue, in our view. Besides, TENAGA may also win the case. Thus, we upgrade the stock to OP with unchanged TP of RM14.30.

ICPT surcharge to reduce in 1HCY20. Yesterday, in the Minister's Question Time at the Parliament, the Energy Minister said that while domestic customers are not affected by imbalance cost pass-through (ICPT) surcharge which will be funded by Kumpulan Wang Industri Elektrik (KWIE) amounting to RM62.95m, the non-domestic customers would enjoy a surcharge reduction of 0.55 sen/kWh to 2.00 sen/kWh in 1HCY20 from 2.55 sen/kWh in 2HCY19. This ICPT surcharge is on top of base tariff of 39.45 sen/kWh. So far, the Energy Commission and TENAGA have not made announcement for the new tariff structure yet.

Effective tariff rate to be reduced by 1.3%. The reduction in ICPT surcharge is not unexpected as given the declining trend of fuel costs. In 3QFY19, average coal cost for TENAGA fell to RM301.90/mt against RM356.80/mt in 1HFY19 while average LNG cost also dropped to RM32.75/mmbtu as opposed to RM36.16/mmbtu in 1HFY19. In fact, both fuel prices have fallen below the reference prices of RM315.90/mt for coal and RM35.00/mmbtu for LNG to use for the formulation of base tariff of 39.45 sen/kWh for Regulatory Period (RP) 2 between 2018 and 2020. Should fuel prices continue to trend lower, we may see a lower base tariff in RP3 over 2020-2022.

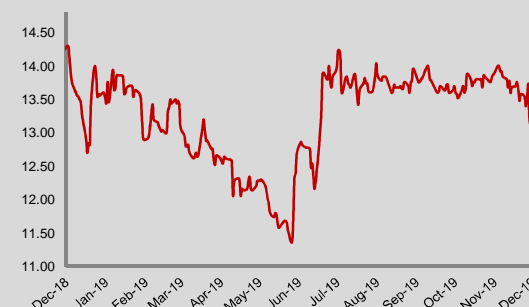
Share price hit by tax dispute. Last Friday, TENAGA faced a heavy sell-down after it was slapped with RM3.98b additional tax assessment by the IRB for 2015-2017. This is the second additional tax assessment after the still unsettled RM2.1b claim which was announced back in Nov 2015. The tax dispute was mainly relating to reinvestment allowance up to 2018. As such, TENAGA may face another dispute claim for 2018 that could amount to another RM1b. However, in our opinion, the sell-down is overdone as this is an isolated event which is not an operational issue. Furthermore, after a good four years, the first dispute is still not settled and TENAGA may also not lose the case while this second dispute could take an even longer time to resolve.

Sell-down overdone; upgrade to OUTPERFORM. We believe the sell-down over the tax dispute is overdone given that it is not an operational issue. At worst, the total dispute claims of up to RM6b could wipe out an entire financial year's earnings but TENAGA may not lose the case. Meanwhile, under the Incentive Based Regulation (IBR) framework with fuel cost past through via ICPT, TENAGA's earnings are expected to be stable with a regulated return of 7.3%. This also offers dividend certainty of c.4% based on 50% payout. As such, the recent sell-down provide further buying opportunity into this heavyweight index-linked stock. Thus, we upgrade the stock to OUTPERFORM from MARKET PERFORM with an unchanged target price of RM14.30 which is based on 3-year moving average of 14x FY20 PER. Risks to our new recommendation are: (i) sharp decline in regulated return rates under new RP3, from 7.3% currently, as well as (ii) a sudden surge in fuel prices resulting in short-term earnings weakness.

OUTPERFORM ↑

Price : **RM13.02**
Target Price : **RM14.30** ↔

Share Price Performance



KLCI 1,562.27
YTD KLCI chg -7.6%
YTD stock price chg -4.3%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	TNB MK
Market Cap (RM m)	74,043.3
Shares outstanding	5,686.9
52-week range (H)	14.30
52-week range (L)	11.24
3-mth avg daily vol:	3,129,778
Free Float	43%
Beta	1.2

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	10,154	10,552
PBT	5,046	7,624	7,687
Net Profit (NP)	3,724	5,754	5,802
Core Net Profit	5,470	5,754	5,802
Consensus (NP)		5,569	5,734
Earnings Revision (%)		-	-
Core EPS (sen)	96.3	101.3	102.2
EPS growth (%)	-10.4	5.2	0.8
NDPS (sen)	53.3	50.7	51.1
BV/Share (RM)	10.2	10.7	11.2
NTA/Share (RM)	10.1	10.7	11.2
Core PER (x)	13.5	12.8	12.7
PBV (x)	1.3	1.2	1.2
Price/NTA (x)	1.3	1.2	1.2
Net Gearing (x)	0.51	0.43	0.35
Net Yield (%)	4.1	3.9	3.9

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Income Statement

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Revenue	47417	15827	50393	52017	52960
EBITDA	15469	5199	14762	20175	21064
Depreciation	-6105	-2050	-6491	-10021	-10511
Operating Profit	9364	3149	8271	10154	10552
Other Income	238	134	424	493	539
Interest Expense	-1456	-576	-1689	-3224	-3604
Associate	128	-37	-189	200	200
Excep. Items	0	0	-1354	0	0
PBT	8282	2979	5046	7624	7687
Taxation	-1370	-235	-1301	-1830	-1845
Minority Interest	-8	12	-21	-40	-40
Net Profit	6904	2756	3724	5754	5802
Core Net Profit	6067	2036	5470	5754	5802

Balance Sheet

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Fixed Assets	103084	104808	111446	111424	110913
Intangible Assets	211	211	241	240	240
Other FA	11197	11522	11259	11450	11450
Inventories	829	885	1296	872	874
Receivables	9104	10510	10381	8733	8891
Other CA	12532	10927	10722	10780	10780
Cash	5056	5415	8370	9727	11540
Total Assets	142012	144277	153714	153227	154688
Payables	11335	10198	10995	9941	9978
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	60715	63616
Share Capital	11125	11200	11446	11446	11446
Reserves	45987	46005	46392	49269	52170
Equity	57111	57205	57838	60715	63616

Cashflow Statement

FY Dec (RM m)	Aug-17	Dec-17	2018	2019E	2020E
Operating CF	11631	1526	11666	16375	16475
Investing CF	-12842	-2008	-10414	-10000	-10000
Financing CF	2295	843	402	-5069	-4661
Change In Cash	1084	361	1655	1306	1813
Free CF	-1211	-482	1253	6375	6475

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

Source: Kenanga Research

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	36.7	4.4
Operating Profit (%)	3.2	0.9	-12.4	22.8	3.9
PBT (%)	2.7	7.9	-43.5	51.1	0.8
Net Profit (%)	-6.3	19.7	-55.0	54.5	0.8
Core Net Profit (%)	-9.3	0.7	-10.4	5.2	0.8

Profitability (%)

EBITDA Margin	32.6	32.8	29.3	38.8	39.8
Operating Margin	19.7	19.9	16.4	19.5	19.9
PBT Margin	17.5	18.8	10.0	14.7	14.5
Net Margin	14.6	17.4	7.4	11.1	11.0
Core Net Margin	12.8	12.9	10.9	11.1	11.0
Effective Tax Rate	40.9	26.8	23.6	25.8	24.0
ROE	11.1	10.7	9.5	13.3	9.3
ROA	5.5	5.5	4.8	7.7	6.1

DuPont Analysis

Net Margin (%)	14.6	17.4	7.4	11.1	11.0
Assets Turnover (x)	0.3	0.1	0.3	0.3	0.3
Leverage Factor (x)	2.5	2.5	2.7	2.5	2.4
ROE (%)	12.1	4.8	6.4	9.5	9.1

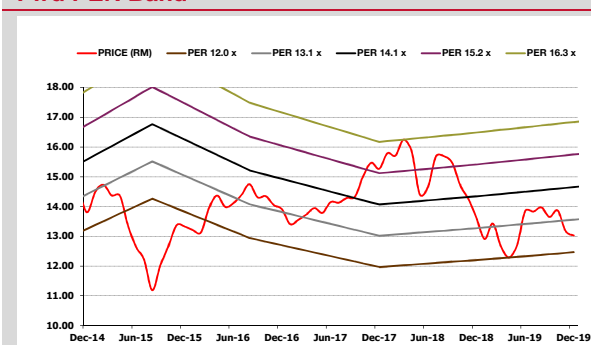
Leverage

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	-25853	-22220
Net Debt/Equity (x)	0.38	0.45	0.51	0.43	0.35

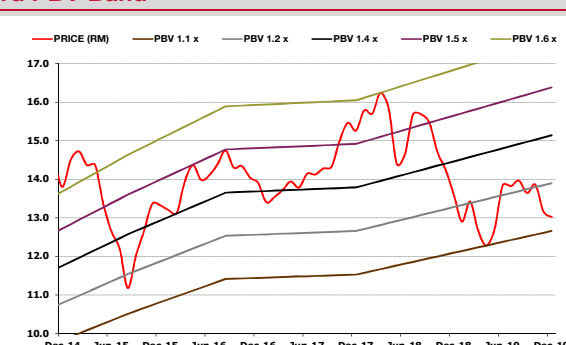
Valuations

EPS (sen)	106.8	35.9	96.3	101.3	102.2
NDPS (sen)	61.0	21.4	53.3	50.7	51.1
BV/share (RM)	10.1	10.1	10.2	10.7	11.2
NTA/share (RM)	10.0	10.0	10.1	10.7	11.2
PER (x)	13.0	12.9	14.4	12.8	12.7
Net Yield (%)	4.7	1.6	4.1	3.9	3.9
P/BV (x)	1.3	1.3	1.3	1.2	1.2
P/NTA (x)	1.3	1.3	1.3	1.2	1.2
EV/EBITDA (x)	6.2	6.1	6.8	4.9	3.5

Fwd PER Band



Fwd PBV Band



Source: Bloomberg, Kenanga Research

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Peer Comparison

Name	Last Price	Market Cap	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price	Rating
	(RM)	(RM'm)			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.	(RM)	
GAS MALAYSIA BHD	2.71	3,479.6	Y	12/2019	5.2%	7.7%	5.9%	4.4%	20.5	19.3	18.5	3.4	3.3	17.4%	4.6%	3.00	MP
MALAKOFF CORP BHD	0.865	4,227.2	Y	12/2019	-0.3%	-0.1%	10.5%	4.5%	19.7	17.8	17.1	0.8	0.8	4.3%	4.5%	1.00	OP
PESTECH INTERNATIONAL BHD	1.27	970.7	Y	06/2020	17.3%	10.5%	25.8%	13.5%	13.4	10.7	9.4	2.1	1.8	18.3%	0.0%	1.75	OP
PETRONAS GAS BHD	15.50	30,670.3	Y	12/2019	4.8%	-1.8%	5.7%	-14.7%	16.8	15.9	18.6	2.4	2.2	14.5%	4.4%	15.75	MP
TENAGA NASIONAL BHD	13.02	74,043.3	Y	12/2019	3.2%	1.8%	5.2%	0.8%	13.5	12.8	12.7	1.3	1.2	9.7%	3.9%	14.30	OP
YTL POWER INTERNATIONAL BHD	0.680	5,219.2	N	06/2020	-12.9%	1.9%	-21.5%	-1.4%	7.9	10.1	10.3	0.4	0.4	3.8%	7.4%	0.700	MP
Simple Average					2.9%	3.3%	5.3%	1.2%	15.3	14.4	14.4	1.7	1.6	11.3%	4.1%		

Source: Bloomberg, Kenanga Research

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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.**

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