Malaysia Airports Holdings

Fair Capex Recovery Mechanism

By Raymond Choo Ping Khoon l pkchoo@kenanga.com.my

Under the new operating agreement (OA) signed with the government recently, AIRPORT has the flexibility to fund airport development via any investment recovery model or bankable financing model agreeable to both parties. This alleviates the concern of AIRPORT having to undertake "national service". We maintain our forecasts, TP of RM9.00 and MARKET PERFORM call.

We came away from AIRPORT's analyst briefing yesterday feeling reassured that it is getting a fair deal out of the new OA signed with the government recently. The key takeaways are as follows:

1. AIRPORT highlighted that overall; the recently signed new OA with the government is net positive with some enhancements compared to the previous OA. The government has the right to restructure the airport industry through clustering, carving out, divestment of airports, closure of existing airports or terminals or the restructuring of the ownership of the facilities subject to the mutual agreement with AIRPORT. Stipulated in the OA, AIRPORT can renegotiate for a lower user fee which currently is 13.11% (escalate 25 basis points per annum) to fund smaller airports. Moreover, unlike the previous OA, the government and AIRPORT now have the flexibility to fund airport development via any investment recovery model or bankable financing model with a weighted average cost of capital (WACC) agreeable to both parties;

2. The potential for AIRPORT to recover future capex with the introduction of cost-based mechanism in Regulatory Period 2 (RP2) starting Jan 2027 removes the risk of uncompensated capex spending. In the new OA, it was highlighted that MAVCOM had also announced that it will adopt a cost-based regulation from 2027 onwards. We believe capex burden may be alleviated or recouped later via the cost-based mechanism (CBM) in setting airport charges.

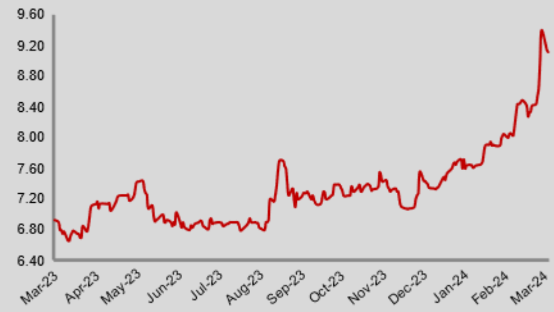
   For illustration purposes, assume AIRPORT plans to expand ABC Airport at an estimated cost of RM1.0b. The state government fund RM0.4b for public infrastructure works, leaving the capex of RM0.5b of which AIRPORT will have to spend upfront, but then is allowed by the federal government via the new OA to claim back over a period of 6-8 years by way of reducing the future user fee payments to the federal government. The net capex spent by AIRPORT of RM100m, in this illustration, can be subsequently recovered by MAHB via the Cost-Based Framework (CBF) mechanism.

3. We are positive on the loss accumulation and recovery mechanisms with an indicative assumed WACC of 11.44%. However, the loss accumulation recovery mechanism will mean AIRPORT cash flow is back loaded. In anticipation that AIRPORT is expected to incur losses following the slow recovery for air travel post pandemic, the OA allows AIRPORT to recover its losses in RP1 via a loss capitalisation mechanism (LCM) starting from Regulatory Period 2 (RP2), The LCM will be applicable to allow MAHB and the operators to recover a proportion of regulatory losses in RP1 (Jun 2024 – 31 Dec 2026) over ten years, beginning 2027. The loss refers to the difference between: (a) an estimate of the revenue that AIRPORT would require over RP1 to cover its prudent and efficient costs (the allowed revenue), and (b) the revenue that AIRPORT will actually earn over RP1 from the imposition of aviation service charges (the actual revenue).

MARKET PERFORM ↔

Price :	**RM9.12**
Target Price :	**RM9.00 ↔**

Share Price Performance



KLCI	1,535.79
YTD KLCI chg	5.6%
YTD stock price chg	23.9%

Stock Information

Shariah Compliant	No
Bloomberg Ticker	MAHB MK
Market Cap (RM m)	15,217.2
Shares Outstanding	1,668.6
52-week range (H)	9.45
52-week range (L)	6.59
3-mth avg. daily vol.	3,118,786
Free Float	45%
Beta	1.2

Major Shareholders

Khazanah Nasional Bhd	33.2%
Employees Provident Fund Board	7.0%
KWAP	6.8%

Summary Earnings Table

FYE Dec (RM m)	2023A	2024F	2025F
Turnover	4,914	5,331	5,920
PBT	506	790	903
Net Profit / Loss	543	592	677
Core NP / NL	443	592	677
Consensus NP/NL	-	763	893
Earnings Revision	-	-	-
Core EPS (sen)	26.7	35.7	40.8
Core EPS Growth (%)	(223.4)	33.7	14.3
NDPS (sen)	10.8	18.0	18.5
BV/Share (RM)	4.82	5.00	5.22
Core PER (x)	34.2	25.6	22.4
Net Gearing (x)	0.3	0.3	0.2
Dividend Yield (%)	1.2	2.0	2.0

For illustration purposes, assume that over RP1, AIRPORT's reveal that it incurred operating costs of RM200m and depreciation of RM500m, and suppose the Commission estimates that AIRPORT should be allowed a return of a further RM500m (to reflect a reasonable rate of return on the unrecovered cost of invested capital). In this case, AIRPORT's allowed revenue for RP1 would be RM1.2b, which is the sum of its operating costs, depreciation, and allowed return on capital. That is, MAVCOM estimates that AIRPORT would need to earn RM1.2b over RP1 to cover its costs. At the start of RP2, MAVCOM would compare this total allowed revenue for RP1 with AIRPORT's actual revenue for RP1. Assuming AIRPORT actually earns RM1.3b over RP1, it earned RM100m more that it required to cover its costs. In this case, AIRPORT would be entitled to retain 10% of the gain (i.e. RM10m) but would be required to return 90% of the gain (i.e., RM90m) to customers via proportionately lower charges over the 'payback' period. Conversely, assume that AIRPORT actually earns RM1b over RP1, which is RM200m less than it required to cover costs. In this case, AIRPORT would be required to bear 10% of this loss (i.e., RM20m) but would be entitled to recover 90% of the loss (i.e., RM180m) from customers through proportionately higher charges over the 'payback' period.

Forecasts. Maintained.

Valuations. We also maintain our TP of RM9.00 based on 22x FY25F EPS at a 40% discount to its closest peer Airport of Thailand due to its smaller market capitalisation. Note that Thailand's tourism revenue is 3x larger than Malaysia's. There is no adjustment to TP based on ESG given a 3-star rating as appraised by us (see Page 4).

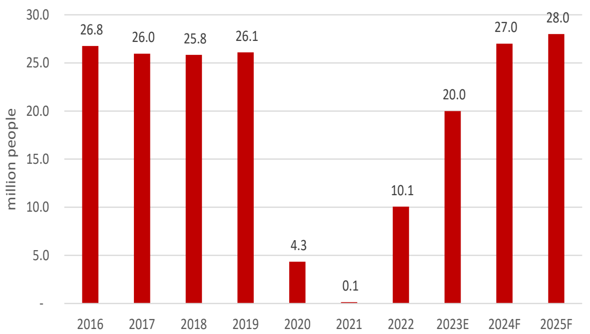
Outlook. We expect business and leisure air travel to continue to recover throughout FY24. According to our in-house projection, tourist arrivals in Malaysia are expected to jump 35% to 27m (consistent with Tourism Malaysia's projection to return to pre-pandemic levels) in FY24 from an estimated 20m a year ago (see Exhibit 2). A key driver is Chinese tourists that had historically contributed to an estimated 12% of total tourist arrivals in Malaysia. Furthermore, tourist arrivals is expected to be boosted by the 30-day visa-free regime for Chinese and Indian visitors to Malaysia starting from Dec 2023 and China, allowing Malaysian inbound visitors 15 visa-free days between 1 Dec 2023 and 30 Nov 2024.

This should underpin growth in AIRPORT's passenger throughput demand in 2024. We expect traffic trajectory to grow in subsequent months as airlines continue to re-activate more aircrafts to match increasing demand. Amplifying traffic growth trajectory is aircraft movements that are pointing towards increased medium and long-haul flights to Perth, Sydney and Auckland, Southeast Asia and South Asia destinations. KL International Airport saw the return of Kuwait Airways after a seven-year hiatus, while two other foreign carriers i.e. KLM Royal Dutch Airlines and All Nippon Airways, will resume non-stop flight operations to Amsterdam and Tokyo, respectively, after temporarily ceasing operations due to the COVID-19 pandemic. In addition, Malaysia Airlines has increased its flight frequency to Tokyo from November 2022, meeting the surge in travel demand after Japan reopened its borders to international travellers. AirAsia Group meanwhile is focusing on its medium-haul operations and had increased its Malaysia AirAsia X flights to 44 times weekly across 10 routes from Nov 2022.

Investment case. We like AIRPORT for: (i) it being the dominant airport operator in Malaysia and one of the largest in Türkiye, (ii) being a good proxy to the recovery of air travel and tourism locally, regionally and globally, and (iii) its strong shareholders who have demonstrated unwavering support through thick and thin (including during the pandemic and a massive cash call in 2014). The recently announced tariff revision is positive to its earnings but may not be sufficient for it to fund more aggressive capex plans. Maintain **MARKET PERFORM**.

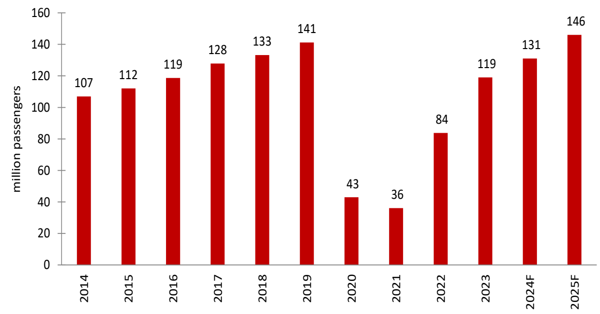
Risks to our call include: (i) endemic and pandemic occurrences, deterring air travel, (ii) unfavourable terms for airport operations, and (iii) risks associated with overseas operations.

Exhibit 1: Tourist Arrivals in Malaysia



Source: Tourism Malaysia, Kenanga Research

Exhibit 2: AIRPORT's Passenger Throughput*



**million passengers*
Source: Kenanga Research, Company

Income Statement

FY Dec (RM m)	2022A	2023A	2024F	2025F
Revenue	3,127.0	4,914.2	5,331.0	5,919.6
EBITDA	1,186.3	2,285.6	2,517.6	2,565.5
Depre. & Amort	(907.3)	(951.3)	(1,133.5)	(1,124.7)
Operating Profit	349.2	2,602.9	1,384.1	1,440.8
PBT	184.6	506.1	789.5	902.7
Taxation	(58.2)	37.1	(197.4)	(225.7)
Net Profit	187.2	543.2	592.1	677.0
Core net profit	(358.8)	442.9	592.1	677.0

Balance Sheet

FY Dec (RM m)	2022A	2023A	2024F	2025F
Fixed Assets	550	603	603	333
Intangibles	14,580	14,663	13,830	13,830
Other FA	251	269	327	391
Inventories	1,484	1,611	1,611	1,611
Receivables	98	127	176	195
Derivatives	536	789	846	1,150
Other CA	29	46	46	46
Financial assets	393	502	502	502
Cash	1,530	1,845	2,273	2,716
Total Assets	19,450	20,455	20,214	20,773
Payables	1,255	1,552	1,552	1,590
ST Borrowings	697	1,249	1,249	1,249
Ot. ST Liability	906	1,080	1,080	1,080
LT Borrowings	4,144	3,338	3,338	3,338
Ot. LT Liability	5,022	5,236	4,759	4,968
Net Assets	7,426	8,000	8,236	8,548
Share Capital	5,114	5,171	5,171	5,171
Reserves	2,312	2,829	3,065	3,377
Equity	7,426	8,000	8,236	8,548

Cashflow Statement

FY Dec (RM m)	2022A	2023A	2024F	2025F
Operating CF	1,040	1,679	2,021	1,828
Investing CF	239	(287)	147	161
Financing CF	(1,360)	(1,268)	(1,018)	(2,042)
Change In Cash	(82)	124	1,150	(53)
Free CF	650	801	2,155	1,975

Financial Data & Ratios

FY Dec	2022A	2023A	2024F	2025F
Growth				
Turnover	86.9%	57.2%	8.5%	11.0%
EBITDA	438.5%	92.7%	10.2%	1.9%
Operating Profit	-188.5%	645.4%	-46.8%	4.1%
PBT	-117.7%	174.1%	56.0%	14.3%
Net Profit /(loss)	-53.2%	-223.4%	33.7%	14.3%
Profitability				
EBITDA Margin	37.9%	46.5%	47.2%	43.3%
Operating margin	-23.6%	53.0%	26.0%	24.3%
PBT Margin	5.9%	10.3%	14.8%	15.2%
Core Net Margin	-11.5%	9.0%	11.1%	11.4%
Eff. Tax Rate	31.5%	-7.3%	25.0%	25.0%
ROA	1.0%	2.7%	2.9%	3.3%
ROE	2.5%	6.8%	7.2%	7.9%
DuPont Analysis				
Net Margin (%)	-11.5%	9.0%	11.1%	11.4%
Assets T/O (x)	0.2	0.1	0.1	0.1
Lev. Factor (x)	0.2	0.2	0.3	0.3
ROE (%)	2.5%	6.8%	7.2%	7.9%
Leverage				
Debt/Asset (x)	0.2	0.2	0.2	0.2
Debt/Equity (x)	0.7	0.6	0.6	0.5
Valuations				
EPS (sen)	11.3	32.7	35.7	40.8
NDPS (sen)	4.0	10.8	18.0	18.5
BVPS (RM)	4.48	4.82	4.96	5.15
PER (x)	80.8	34.2	25.6	22.4
Net Div. Yield (%)	0.4	1.2	2.0	2.0
PBV (x)	2.1	1.9	1.9	1.8

Source: Kenanga Research, Bursa Malaysia, Bloomberg

Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★		
	Community Investment Workers Safety & Wellbeing	★	★	★		
	Corporate Governance	★	★	★		
	Anti-Corruption Policy	★	★	★		
	Community Investment Workers Safety & Wellbeing	★	★	★		
	Corporate Governance	★	★	☆		
SPECIFIC	Airport Service Quality (ASQ)	★	★	★	★	
	Cybersecurity/Data Privacy	★	★	★		
	Customer Experience	★	★	★		
	Supply Chain Management	★	★	★		
	Energy Efficiency	★	★	★		
	Effluent/Waste Management	★	★	☆		
	OVERALL	★	★	★		

☆ denotes half-star
★ -10% discount to TP
★★ -5% discount to TP
★★★ TP unchanged
★★★★ +5% premium to TP
★★★★★ +10% premium to TP

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.***

Published 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