Utilities

NEUTRAL

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Upside Exhausted, Hold for Yields

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We remain NEUTRAL on the sector. The sector offers earnings defensiveness backed by regulated assets, offering dividend yields of 3% to 6%. However, most key stocks are fully valued after the recent run-up in their share prices. TENAGA (MP; TP: RM11.50) guided for electricity demand growth of 2.5% to 3.0% in CY24, driven by additional demand from new data centres. Meanwhile, stabilising coal prices mean that negative fuel margin, which blew a big hole in power producers' earnings in CY23, is unlikely to recur in CY24, while normalising gas prices will have a mixed impact on gas utilities. Our top sector pick is YTLPOWR (OP; TP: RM4.20) for its PowerSeraya's earnings bonanza and long-term growth driven by its data centre and digital banking ventures.

A data centre play. TENAGA guided for electricity demand growth of 2.5% to 3.0% in Peninsular Malaysia in CY24, vs. 3.6% achieved in CY23 (which was partly driven by the economy reopening). The key driver for CY24 electricity demand growth is the onboarding of data centres completed in CY23 with a combined capacity of c.635MW. In addition, nine more data centre projects with a combined capacity of c.700MW are expected to be completed this year. **TENAGA** projects a total potential demand of >5,000MW of electricity annually from data centres by CY35.

In terms of energy sources, **TENAGA** is transitioning to green energy with a pipeline of green energy project with a combined capacity of c.7,700MW comprising hydro plants, hybrid hydro-floating solar PV, hydrogen-ready combined cycle power plant, corporate green power program and large-scale solar parks. In FY24, the energy transition capex is budgeted at RM3.33b. Meanwhile, it also needs to upgrade the transmission and distribution (T&D) system including power grid to meet the demand from the growing renewable energy (RE) assets. It also means that a higher T&D capex will increase **TENAGA**'s regulated asset base (RAB), resulting in higher absolute earnings based on a return pegged to WACC of 7.3% under the Regulatory Period 3 (RP3). **TENAGA** has set aside RM7b capex in FY24 for its regulated business and RM5b-RM6b for non-regulated power generation business such as solar farms and hydropower plants.

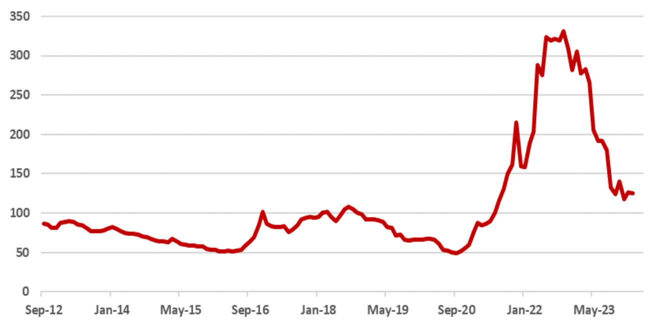
Stable fuel prices. Fuel prices for coal and gas have been fairly benign in the past six months as opposed to sharp surge in 2HCY22 and sudden collapse in 1HCY23. As a result, **TENAGA's** receivables, including Imbalance Cost Pass-through (ICPT) receivables were reduced substantially by 56% to RM9.7b in 4QFY23 from the peak of RM22.0b in 4QFY22. The shrinking ICPT receivables will result in lower working capital requirements and hence lower interest expenses and better earnings going forward for **TENAGA.** On the other hand, stabilising coal prices mean that negative fuel margin which blew a hole in power producers' earnings in CY23 is unlikely to recur in CY24. To recap, the total negative fuel margin cost for **TENAGA** and **MALAKOF (MP; TP: RM0.68)** in FY23 were RM618.7m and RM828.2m, respectively.

Mixed impact on gas utilities. While the movement of gas prices has neutral impact in the longer run given the regulated framework, the current declining gas price trend has a positive impact on **PETGAS (MP; TP: RM17.87)** in the immediate term as low gas price leads to lower internal gas consumption (input cost) for its regulated business as well as non-regulated utilities segment. The utilities segment uses gas as fuel to generate and supply power, stream and industrial gasses to industries. However, weaker gas prices work against **GASMSIA's (MP; TP: RM3.33)** non-regulated retail margins, which are calculated based on a fixed percentage on the gas selling price. On the other hand, **YTLPOWR's** solid earnings from PowerSeraya is expected to sustain at least in the next two years, underpinned by favourable retail prices against gas input cost locked in at low cost (during the early days during the pandemic) while it expects a maiden earnings contribution from data centre in 4QFY24 (FYE: Jun).

We raise our FY24-25F net profit forecasts for **TENAGA** by 1% each to bring ourselves more in line with its guidance for electricity demand growth. We now assume electricity demand growth of assumption of 2.5% in FY24-25 (vs. 1.8% previously) and lift our TP to RM11.50 (from RM11.40).

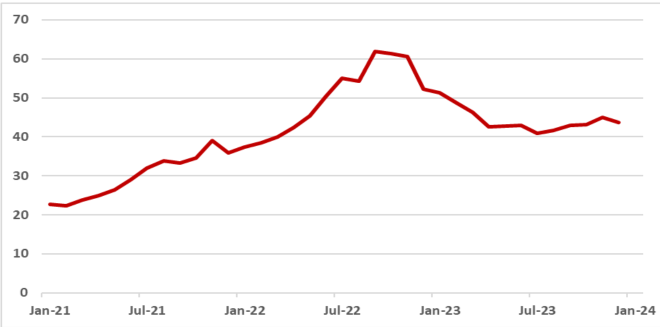
We remain **NEUTRAL** on the sector. The sector offers earnings defensiveness backed by regulated assets, offering dividend yields of 3% to 6%. However, most key stocks are fully valued after the recent run-up in their share prices. Our sector top pick is **YTLPOWR** for: (i) its earnings stability backed by various regulated assets globally, (ii) the strong near-term earnings prospects of PowerSeraya backed by gas inventory locked in at low prices, and (iii) its longer-term growth potential from its data centre and digital banking ventures.

Indonesia Coal Benchmark Price (USD)



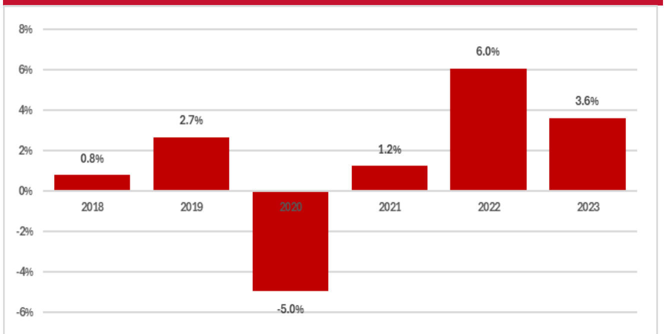
Source: Bloomberg

Malaysia Reference Price (RM)



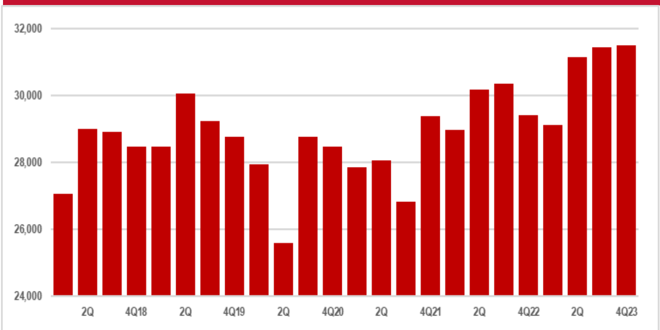
Source: DOSM

TENAGA: Annual Electricity Demand Growth



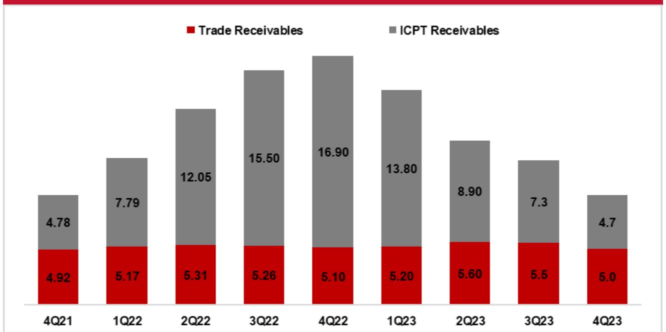
Source: Tenaga

TENAGA: Monthly Electricity Sales (GWh)



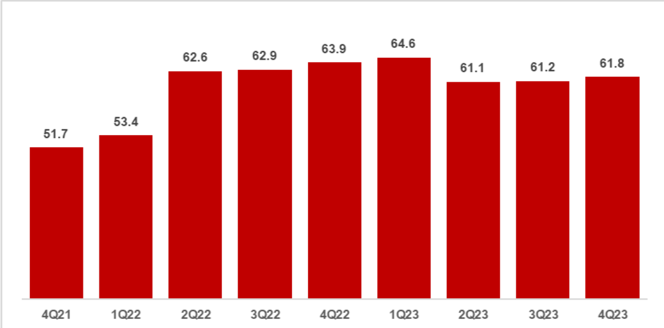
Source: Tenaga

TENAGA: Trade & Other Receivables (RM b)



Source: Tenaga

TENAGA: Borrowings (RM b)



Source: Tenaga

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net. Div. (sen)	Net Div Yld
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
GAS MALAYSIA BHD	MP	3.52	3.33	-5.4%	4,519.7	Y	12/2024	25.7	24.4	-13.8%	-5.2%	13.7	14.4	3.1	23.4%	20.6	5.9%
MALAKOFF CORP BHD	MP	0.645	0.680	5.4%	3,152.1	Y	12/2024	4.7	5.8	-71.9%	24.1%	13.7	11.1	0.7	5.2%	3.8	5.8%
PETRONAS GAS BHD	MP	18.02	17.87	-0.8%	35,656.7	Y	12/2024	98.4	100.7	5.2%	2.4%	18.3	17.9	2.6	14.2%	72.0	4.0%
SAMAIDEN GROUP BHD	OP	1.36	1.51	11.0%	564.7	Y	06/2024	3.7	5.3	33.6%	43.7%	37.0	25.7	5.4	15.7%	0.0	0.0%
SOLARVEST HOLDINGS BHD	OP	1.56	1.88	20.5%	1,045.7	Y	03/2024	4.1	6.9	52.8%	67.4%	37.6	22.5	4.8	13.8%	0.0	0.0%
TENAGA NASIONAL BHD	MP	11.52	11.50	-0.2%	66,670.1	Y	12/2024	73.7	79.5	37.4%	7.9%	15.6	14.5	1.1	7.0%	36.5	3.2%
YTL POWER INTERNATIONAL BHD	OP	4.01	4.10	2.2%	32,497.3	N	06/2024	35.3	28.1	45.9%	-20.5%	11.4	14.3	1.8	16.5%	6.0	1.5%
Sector Aggregate					**144,106.3**					**49.2%**	**-1.5%**	**14.9**	**15.1**	**2.8**	**13.7%**		**2.9%**

Source: 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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