

COMPANY UPDATE

Tenaga Nasional (TNB MK)

Focus On Operational Efficiency As TNB Enters Mid-regulatory Cycle

TNB has received RM9b (out of RM10b) in imbalance cost pass-through to date. With this, together with declining coal prices and the government's commitment towards targeted subsidies, TNB is set to benefit from improving cashflow and balance sheet position. As TNB enters its second year of the regulatory period, the key focus is on operational efficiency. We understand that there is lower forced outage in 2Q23 for TNB Genco. Maintain BUY. Target price: RM10.40.

WHAT'S NEW

- **Easing working capital requirement bodes well for TNB.** To date, the company has received RM9.13b (out of RM10.4b) from the government as compensation for higher 1H23 fuel costs. The balance of RM1.28b is likely to be paid within the next few weeks. Together with: a) declining global coal prices, and b) the government's commitment towards targeted subsidies, we expect Tenaga Nasional Berhad's (TNB) trade receivables to improve from here on. This is in line with a decline in trade receivables owed by the government which is expected to ease from RM13.8b (Mar 23) to RM10b (Jun 23).
- **The government remains committed to targeted subsidies.** The government announced 2H23 electricity tariffs that were well within expectations. This includes a 10 sen/kwh surcharge (20% increase) to consumers with usage above 1,500 kwh/month. The average commercial and industrial user will experience a 17 sen/kwh surcharge for 2H23 – a drop from the 20 sen/kwh surcharge in 1H23. We are positive on this as it implies the government's commitment towards the incentive-based regulation (IBR) framework. This paves the way for a healthy balance sheet and sustainable dividend yield of c.5% for TNB.
- **Second year of RP3.** 2023 is the mid-point for TNB's Regulatory Period 3 (RP3) (2023-24) and the main focus is on execution in terms of capex planning and operational excellence. The regulatory returns for RP3 are stable at 7.3%. Importantly, TNB has been able to demonstrate world-class network performance (see overleaf performance indicator for 1Q23). We understand that TNB Genco is also faring well in 2Q23, as there is lower forced outage in the quarter. We expect plant availability to improve qoq as 1Q23 equivalent plant availability factor (EAF) is only at 84.41%.

KEY FINANCIALS

Year to 31 Dec (RMm)	2021	2022	2023F	2024F	2025F
Net turnover	52,630	73,183	56,607	57,505	58,413
EBITDA	19,412	19,141	21,453	21,669	20,818
Operating profit	8,721	7,738	9,769	10,235	9,796
Net profit (rep./act.)	3,662	3,463	4,864	5,080	5,314
Net profit (adj.)	5,141	4,703	4,864	5,080	5,314
EPS (sen)	90.4	82.7	85.5	89.3	93.4
PE (x)	10.0	10.9	10.6	10.1	9.7
P/B (x)	0.9	0.9	0.9	0.9	0.9
EV/EBITDA (x)	6.1	6.2	5.5	5.4	5.7
Dividend yield (%)	4.4	5.1	5.1	5.4	5.5
Net margin (%)	7.0	4.7	8.6	8.8	9.1
Net debt/(cash) to equity (%)	76.5	100.8	113.2	92.3	77.7
Interest cover (x)	5.6	4.5	5.1	4.9	5.6
ROE (%)	6.5	6.0	8.5	8.9	9.0
Consensus net profit	-	-	4,707	4,807	4,953
UOBKH/Consensus (x)	-	-	1.03	1.06	1.07

Source: Tenaga Nasional, Bloomberg, UOB Kay Hian

BUY

(Maintained)

Share Price	RM9.05
Target Price	RM10.40
Upside	+14.9%

COMPANY DESCRIPTION

Generates and distributes electricity in Peninsular Malaysia and Sabah.

STOCK DATA

GICS sector	Utilities
Bloomberg ticker:	TNB MK
Shares issued (m):	5,787.3
Market cap (RMm):	52,375.4
Market cap (US\$m):	11,223.7
3-mth avg daily t'over (US\$m):	8.9
Price Performance (%)	

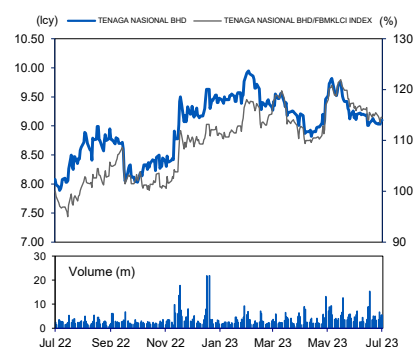
52-week high/low RM9.95/RM7.89

1mth	3mth	6mth	1yr	YTD
(4.8)	(2.0)	(6.0)	13.4	(6.0)

Major Shareholders

	%
Khazanah Nasional	25.8
PNB	18.1
EPF	16.7
FY23 NAV/Share (RM)	9.81
FY23 Net Debt/Share (RM)	11.10

PRICE CHART



Source: Bloomberg

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STOCK IMPACT

- **Higher RE targets...** The group has a target of 8.3GW of renewable energy (RE) capacity to be achieved by 2025. This is dependent on the opportunities available in the market with Vantage RE (a wholly-owned subsidiary) scouting for projects in both the UK and Europe. The group is open to both brownfield and greenfield projects.
- **... means that TNB's grid must be ready in RP4 capex budget.** The increasing renewable energy mix (Malaysia targets to increase RE mix from the current 25% to 70% by 2050) suggests there is a need for a nimble gridline. This is because RE is intermittent and the gridline needs to be able to manage the surge or drop in electricity flow at any point in time. As such, TNB guided for a smart grid in the RP4 budget. This is a requirement as Malaysia transitions to a greener energy landscape.

EARNINGS REVISION/RISK

- **No change to earnings.** We project 2023-24 net profits at RM4,864m and RM5,080m respectively. This is premised on a 7.3% return on asset for TNB's transmission and distribution assets (which account for more than 85% of the group's net profit).
- **Cashflow and dividend management.** As the company focuses on operational efficiency, cashflow is expected to be stable given declining coal prices and easing working capital constraints. The company remains committed to paying at least 30-60% of its net profit as dividends. We expect the stock to yield 5% over 2023-25F.

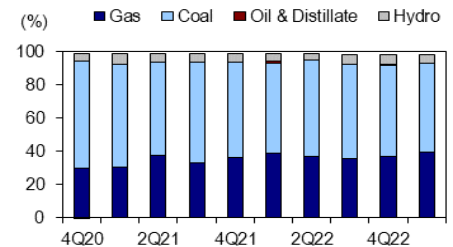
VALUATION/RECOMMENDATION

- **Maintain BUY** on share price weakness for good earnings visibility and sustainable yield. Key re-rating catalysts include: a) allowing TNB the autonomy to change electricity prices by 7% without seeking Cabinet approval every six months, b) listing of TNB Genco, and c) earnings-accretive M&As. Key risks: a) lumpy and unprofitable overseas RE projects, and b) forex risk to operating cashflow.
- **TNB Genco listing earliest in 2025.** It was previously reported in the media that the company was planning a US\$1b IPO for TNB Genco. While we believe the separate listing of TNB's entities is positive for the stock, the listing exercise will only happen sometime in 2025 (ie not in the next 12-18 months). We understand that TNB Genco needs at least three years of operational history before a submission can be made. In 2022, TNB Genco reported a 30% yoy jump in net profit to RM861m. This is due to higher fuel margin earned by TNB's coal-fired power plants.

ENVIRONMENTAL, SOCIAL, GOVERNANCE (ESG)

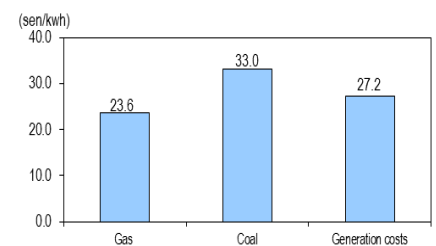
• Environmental <ul style="list-style-type: none"> - Besides targeting to have 8,300MW of RE generation capacity by 2025 (1.5x from 3,398MW in Dec 20), TNB has also made new pledges to reduce emission intensity by 2035 and achieve zero net emission on top of being coal-free by 2050. 	
• Social <ul style="list-style-type: none"> - TNB has donated: a) around RM4.36m to those affected by COVID-19, b) necessary medical supplies, such as ventilators, respirators and personal protective equipment (PPE) to government hospitals, departments, and agencies totalling RM27.5m in 2020, and c) RM1m for lighting up security official posts during MCO enforcement throughout the nation from Mar-Nov 20. 	
• Governance <ul style="list-style-type: none"> - Good company transparency along with an anti-bribery and whistle-blowing policy. - Succession planning is also in place. 	

GENERATION MIX



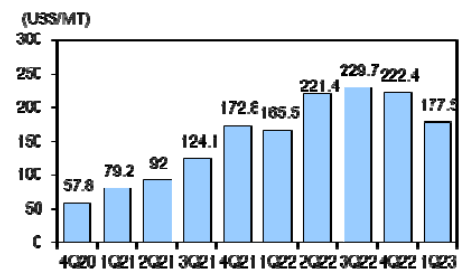
Source: TNB, UOB Kay Hian

GENERATION UNIT COST (1Q23)



Source: TNB, UOB Kay Hian

QUARTERLY COAL PRICES



Source: TNB, UOB Kay Hian

1Q23 TECHNICAL PERFORMANCE FOR TNB



Source: TNB

PROFIT & LOSS

Year to 31 Dec (RMm)	2022	2023F	2024F	2025F
Net turnover	73,183	56,607	57,505	58,413
EBITDA	19,141	21,453	21,669	20,818
Deprec. & amort.	11,403	11,684	11,434	11,022
EBIT	7,738	9,769	10,235	9,796
Total other non-operating income	966	940	940	940
Associate contributions	98	102	108	113
Net interest income/(expense)	(4,213)	(4,201)	(4,383)	(3,733)
Pre-tax profit	5,348	6,610	6,899	7,116
Tax	(1,791)	(1,653)	(1,725)	(1,708)
Minorities	(94)	(94)	(94)	(94)
Net profit	3,463	4,864	5,080	5,314
Net profit (adj.)	4,703	4,864	5,080	5,314

BALANCE SHEET

Year to 31 Dec (RMm)	2022	2023F	2024F	2025F
Fixed assets	116,577	113,893	111,459	107,437
Other LT assets	44,289	44,391	44,499	44,612
Cash/ST investment	4,893	539	9,868	16,234
Other current assets	40,163	39,247	34,567	34,892
Total assets	205,922	198,071	200,393	203,174
ST debt	13,262	13,162	13,062	12,962
Other current liabilities	24,335	19,342	19,476	19,893
LT debt	50,620	50,520	50,420	50,320
Other LT liabilities	56,739	56,739	56,739	56,739
Shareholders' equity	58,517	55,765	58,058	60,529
Minority interest	2,449	2,543	2,637	2,731
Total liabilities & equity	205,922	198,071	200,393	203,174

CASH FLOW

Year to 31 Dec (RMm)	2022	2023F	2024F	2025F
Operating	9,378	7,462	25,699	20,142
Pre-tax profit	349	1,610	6,899	7,116
Tax	(1,791)	(1,653)	(1,725)	(1,708)
Deprec. & amort.	11,403	11,684	11,434	11,022
Associates	(98)	(102)	(108)	(113)
Working capital changes	(10,680)	(4,078)	4,814	92
Non-cash items	0	0	0	0
Other operating cashflows	10,196	0	4,383	3,733
Investing	(14,553)	(9,000)	(8,869)	(5,936)
Capex (growth)	(8,445)	(9,000)	(9,000)	(7,000)
Investments	3	0	0	0
Others	(6,111)	0	131	1,064
Financing	3,896	(2,816)	(7,501)	(7,840)
Dividend payments	(2,616)	(2,616)	(2,787)	(2,843)
Issue of shares	277	0	0	0
Proceeds from borrowings	13,846	(200)	(200)	(200)
Others/interest paid	(7,611)	0	(4,514)	(4,797)
Net cash inflow (outflow)	(1,279)	(4,354)	9,329	6,366
Beginning cash & cash equivalent	6,706	4,893	539	9,868
Changes due to forex impact	(533)	0	0	0
Ending cash & cash equivalent	4,894	539	9,868	16,234

KEY METRICS

Year to 31 Dec (%)	2022	2023F	2024F	2025F
Profitability				
EBITDA margin	26.2	37.9	37.7	35.6
Pre-tax margin	7.3	11.7	12.0	12.2
Net margin	4.7	8.6	8.8	9.1
ROA	1.8	2.4	2.5	2.6
ROE	6.0	8.5	8.9	9.0
Growth				
Turnover	39.1	(22.7)	1.6	1.6
EBITDA	(1.4)	12.1	1.0	(3.9)
Pre-tax profit	12.9	23.6	4.4	3.1
Net profit	(5.4)	40.4	4.4	4.6
Net profit (adj.)	(8.5)	3.4	4.4	4.6
EPS	(8.5)	3.4	4.4	4.6
Leverage				
Debt to total capital	51.2	52.2	51.1	50.0
Debt to equity	109.2	114.2	109.3	104.5
Net debt/(cash) to equity	100.8	113.2	92.3	77.7
Interest cover (x)	4.5	5.1	4.9	5.6

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