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Upside exhausted for utilities sector, hold for yields

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Tenaga guides for electricity demand growth of 2.5 to three per cent in 2024, driven by additional demand from new data centres. — Bernama photo

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Ronnie Teo

KUCHING: The utilities sector offers earnings defensiveness backed by regulated assets, offering dividend yields of three to six per cent.

However, most key stocks are fully valued after the recent run-up in their share prices, based on an analysis by Kenanga Investment Bank Bhd (Kenanga Research).

"Tenaga Nasional Bhd (Tenaga) guided for electricity demand growth of 2.5 to three per cent in 2024, driven by additional demand from new data centres," it said in its review.

"Meanwhile, stabilising coal prices mean that negative fuel margin, which blew a big hole in power producers' earnings in 2023, is unlikely to recur in 2024, while normalising gas prices will have a mixed impact on gas utilities.

"Our top sector pick is YTL Power Bhd for its PowerSeraya's earnings bonanza and long-term growth driven by its data centre and digital banking ventures."

Kenanga Research said the key driver for 2024 electricity demand growth is the onboarding of data centres completed in 2023 with a combined capacity of circa 635MW.

In addition, nine more data centre projects with a combined capacity of about 700MW are expected to be completed this year. Tenaga projects a total potential demand of more than 5,000MW of electricity annually from data centres by 2035.

In terms of energy sources, Tenaga is transitioning to green energy with a pipeline of green energy project with a combined capacity of circa 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 RM3.33 billion. 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 assets.

"It also means that a higher T&D capex will increase Tenaga's regulated asset base, resulting in higher absolute earnings based on a return pegged to WACC of 7.3 per cent under the Regulatory Period 3."

Tenaga has set aside RM7 billion capex in FY24 for its regulated business and RM5 billion to RM6 billion for non-regulated power generation business such as solar farms and hydropower plants.