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# Rise in fuel cost will continue to be earnings neutral for TNB

| ▶ TENAGA NASIONAL BHD | | | | |
|---|---|---|---|---|
| FYE DEC 31 | 2017 | 2018E | 2019E | 2020E |
| **REVENUE** (RM mil) | 15,827.1 | 50,004.1 | 51,229.0 | 52,656.8 |
| **PATAMI** (RM mil) | 2,755.7 | 7,721.1 | 7,535.1 | 7,357.1 |
| **EPS** (sen) | 48.8 | 136.8 | 133.5 | 130.4 |
| **PER** (x) | 29.3 | 10.5 | 10.7 | 11.0 |

## ▶ Recommendation: Buy

TARGET Price: RM18.70
by Affin Hwang Investment Bank Bhd (July 10)

### Highlights

THERE have been calls by a few parties pleading for the government to absorb the recent tariff hike from both domestic and non-domestic users.

We believe that a diversion from the incentive based regulation (IBR)/imbalance cost pass-through (ICPT), would certainly reintroduce uncertainty to the system, and is likely to be negative for Tenaga Nasional Bhd's (TNB) share price and the sector.

Nevertheless, we maintain our view that the government would still follow through with the current system.

**Flip-flopping is not good for TNB.** We believe that flip-flopping on the issue would have long lasting impact on TNB, due to the uncertainty in both the policy and the framework used to determine the tariff. TNB will no doubt be negatively impacted by the decision, as the risk premium associated to its stock and bond are likely to increase.

Lower profitability (higher interest cost) and being less competitive (higher WACC) are some of the negative implications that are associated with the higher risk premium in the long-run.

TNB fitting the bill will be the worst case scenario. There could also be downside risk to earnings, should TNB be asked to share the incremental fuel cost of RM698m for 2H18 (c. 9% of 2018E net profit), despite only close to half of TNB's profit being generated from the D&T segment.

As a result, we believe TNB's share price could revert to the RM7-RM10 stock price range, ie before the implementation of IBR/ICPT in 2014.

Alternatively, there are a few options that the government could explore to alleviate the surcharge, like lowering the natural gas price supplied to the power sector or renegotiate for a capacity payment with the IPPs and TNB.

**Maintain 'Buy' with an unchanged TP at RM18.70.** We are maintaining our 'Buy' call on the stock, with an unchanged DCF-based TP of RM18.70.

In our view, the government is likely to maintain the current ICPT mechanism, and the increase in fuel cost will continue to be earnings neutral to TNB, supporting its current payout. TNB is also our preferred pick for the sector, and one of Malaysia's Top Buy ideas.

Downside risks include the revision of policy and higher than expected losses from its associates and changes to the current IBR/ICPT.