Tenaga in focus amid talks of tariff hike

BY ESTHER LEE

Over a span of two weeks, Tenaga Nasional Bhd’s share price gained close to 5%, closing at RM12.22 last Thursday from RM11.66 on June 12. The share price movement could have been driven by hints of a possible electricity tariff revision made at a briefing by Power Corp Bhd recently.

As the six-monthly tariff review by the Energy Commission (EC) nears, investors and analysts alike are waiting to see whether a decision will be made over the next few weeks. It will be a decision that could boost Tenaga’s earnings going forward. The last tariff hike came in January this year at a quantum of 15% to 38.53 sen per kilowatt-hour (kWh).

Maybank Investment Bank Research in a report estimates a potential hike of up to 3.5% if the tariff hike takes place in July under an optimistic scenario of RM45/mmBtu for 400mmscfd of LNG-sourced gas and US$75/mt for coal.

JP Morgan says in a recent report that it is expecting a rate hike of between 2% and 3%, which could boost Tenaga’s earnings by RM100 million to RM150 million.

Nonetheless, some analysts opine that even without a tariff rate hike, the impact would be neutral for Tenaga should the EC take up MyPower Corp’s proposal to utilise the RM500 million savings it has accumulated from the renegotiations of the power purchase agreements (PPAs) with the independent power producers (IPP). “In my view, if the tariff hike does not happen, the impact will be neutral for TNB if the fuel cost can be compensated by another avenue — the first-generation IPP savings, they have been talking about,” says an analyst.

The analyst adds that if the tariff hike does not happen as expected, it will likely cause some pressure on Tenaga’s share price.

CIMB Research says in a report that while a delay in the expected tariff hike is a setback for Tenaga, the utilisation of the RM500 million savings to mitigate fuel-cost effects is a silver lining for the utility company. Nevertheless, it highlights that the move is merely a “short-term fix” as future tariff revisions remain in uncertain territory.

“The delay in the tariff hike would likely cause Tenaga’s share price to be weaker in the short term. Any weakness would be an opportunity to accumulate, in our view,” says CIMB Research.

However, the crux of the issue still remains, that is, to have a fuel cost pass-through mechanism implemented on a consistent basis, analysts opine.

“In our view, the quantum of the July 2014 tariff is secondary. What is more important is for the EC to make a statement, so as to signal to the market that the fuel-cost pass-through mechanism is in place. This remains our base case,” says Maybank IB Research.

Market observers say that an upward revision this time — given rising fuel costs — would imply that the fuel-cost pass-through mechanism is finally in place and this would bode well for Tenaga’s earnings visibility. Nevertheless, they add that the EC could lack the political will to do so.

According to a fund manager, Tenaga has the potential to ring in RM6 billion in net profits a year, under normal circumstances. However, he thinks the utility company’s earnings this year could come in at RM5.5 billion to RM5.7 billion, as the last electricity tariff hike only took place in January, four months into the company’s financial year.

An analyst highlights that the effects of the January tariff hike will likely be seen in TNB’s next quarterly earnings (3QFY2014 ended May), pointing towards an expectation of better financial results in the coming quarters.

Tenaga’s net profit came in at RM4.61 billion for its financial year ended Aug 31, 2013, and RM3.4 billion for its cumulative six months ended Feb 28, 2014.

“Tenaga has the potential of being the largest company, in terms of earnings, in Malaysia. It could become larger than the financial institutions in Malaysia,” says the fund manager.

Last year, Malayan Banking Bhd, the largest company in Malaysia, raked in RM6.55 billion in net profit for the financial year ended Dec 31, 2013.

Currently, analysts are mostly bullish on Tenaga. Bloomberg data shows that there are 21 “buy” calls, three “hold” and one “sell” on the stock. Target price based on these analysts’ estimates range from RM12.20 to RM16.50 with an estimated FY2014 earnings ratio of some 13 times.

“We continue to be bullish on TNB, as we believe investors have yet to price in the company’s longer-term earnings growth potential. Present expectations merely revolve around a stable earnings base under the incentive-based regulation framework, in our view,” says Maybank IB Research.