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ESG is major concern for TNB's investors

by AZALEA AZUAR

INVESTORS are worried about Tenaga Nasional Bhd's (TNB) recent environmental, social and governance (ESG) engagement session due to its carbon emissions, affordability of electricity and government's emphasis on environmental sustainability, CGS-CIMB Research stated.

TNB expected to announce its sustainable pathway in the second half of 2021 with more details on its long-term commitments and key performance indicators, said analyst Ngo Siew Tang.

"The majority of investors are constantly engaging with TNB to understand its efforts to address the ESG issue; only a few funds are shying away due to the group's coal-related exposure.

"TNB is ranked average among its regional peers, and slightly slower than some of its leading peers, in terms of ESG progress due to its business model, where it has to balance sustainability, affordability and energy security of the electricity supply," said Ngo.

The power utility company has dedicated a team and external consultants for ESG practices to help it identify business opportunities such as batteries from energy transition.

For the period between 2022 to 2024, TNB is proposing a RM25 billion regulated capital expenditure (capex) to benefit from additional grid investments which is higher than Regulatory Period (RP) 2's approved capex of RM19 billion.

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More regulated capex would also be allocated to facilitate energy transition (from RP2's 12% of total capex to 19% for RP3).

"With its natural monopoly position in Malaysia's transmission and distribution, we believe TNB will likely benefit from this trend as these ongoing investments should be part of TNB's regulated asset base, supporting its regulated earnings in future," Ngo added.

Its existing grid infrastructure can dispatch up to 27% of renewable energy (RE) but at the moment only 5% of its dispatched power comes from RE.

She expects TNB to take advantage of growing opportunities in RE as it expands its RE capacity domestically or internationally as a power generator as well as its potential thermal plant bidding in the future due to growing electricity demand from digitalisation.

Moreover, the company should also invest on electricity grids to cater to energy transition, which will grow its regulated asset base.

"Our target price of RM13.40 is based on 15 times financial year 2022 price-to-earnings (P/E) (TNB's five-year historical P/E), which reflects the stock's trading range during the incentive-based regulation period."

To ensure its revenue does not exceed 25% of the total revenue from coal generation plants, TNB would not be investing in greenfield coal plants after the Jimah East Power project.

Therefore, Ngo predicted TNB's coal-related revenue should not exceed 20% by 2030 forecast (2030F) since major coal plants are gradually going offline.

The company needs to reach 8,300MW by 2025F, which also includes its hydro plants.

In December 2020, its RE capacity was a total of 3,398MW (domestic: 2,732MW; international: 666MW).

Its RE growth strategy is focused on international assets in selected growth markets and regions where it already has presence such as the UK, Europe and South-East Asia as well as domestic assets by participating in large scale solar projects, small RE projects and rooftop solar projects.

Out of the target 8,300MW RE capacity, 3,100MW will be coming from domestic locations, 3,400MW from the UK or Europe and 1,800MW from the South-East Asia region.

Upon achieving the RE target, TNB's RE revenue will be 10% of its total revenue (2020: 4% of total revenue) and 32% of its total installed generation capacity by 2025F. We gather the total capex needed will be RM6.5 billion, Ngo stated.

She also expected stronger earnings from associates which would be a key potential in TNB's re-rating catalysts.