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KUALA LUMPUR (June 27): Tenaga Nasional Bhd (TNB) has seen a flurry of analysts lowering their target prices on the utilities giant, after the government announced the decision to maintain the effective electricity tariff for Peninsular Malaysia in a bid to tame increasing costs of living.

According to *Bloomberg* data, six analysts cut their TPs on TNB to between RM6.60 to RM8.90, while two of them also downgraded their ratings on the company. There are a total of 20 analysts covering the stock.

RHB Research analyst Sean Lim, who downgraded TNB to 'neutral' from 'buy', said in a note on Monday that the government's decision was a surprise and will raise regulatory risks for TNB.

While the government has upheld the Imbalance Cost Pass-Through (ICPT) framework in the past to ensure regulatory returns, keeping the tariff rates unchanged will mean a higher burden as fuel prices are still high, he said.

"Although the previous subsidisation of domestic users was funded by the Electricity Industry Fund or KWIE, we are not certain about its sustainability under the current situation," said the analyst, who also cuts target price to RM8.60 from RM11.50.

"In the worst-case scenario where ICPT no longer holds, TNB's defensive earnings could be at risk if it is vulnerable to volatile fuel prices, without being able to fully pass the costs to end-consumers," he added.

On Friday (June 24), Putrajaya announced it was maintaining an electricity tariff surcharge of 3.7 sen per kilowatt hour (kWh) for non-domestic users, while keeping the two sen rebate per kWh for domestic users. The government will bear a subsidy of RM5.8 billion arising from this decision.

The decision bucked general expectations that the electricity surcharge will be raised under the ICPT mechanism's semi-annual review due to the elevated prices for coal, which constitutes over half of Peninsular Malaysia's electricity generation mix.

MIDF Research analyst Hafriz Hezry said the government's decision could also put a strain on TNB's free cash flow, as high fuel price has resulted in TNB significantly under-recovering generation cost,

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which is set to be exacerbated further by a weaker ringgit.

"The government's subsidy alleviates some concern on Tenaga's 1H22 under-recovery. However, given that fuel prices remain elevated moving into 2H22, we still expect TNB under-recovery and working capital requirement to remain elevated, which in turn is expected to pressure free cash flow generation," he said in a separate note.

Hafriz kept a 'neutral' rating on TNB, but cut target price to RM8.45 from RM9.55.

RHB's Lim, meanwhile, said while TNB can claim RM5.8 billion from the government in the second half of this year (2H22), it is still unable to fully cover generation costs incurred in the past year.

"ICPT receivables may still rise if fuel prices remain high, and operating cash flow will be under greater pressure if the government does not pay the subsidy on time," he said, adding that TNB's 1Q22 net gearing was at 0.8 time, and the utilities giant may increase its working capital via untapped credit facilities or a sukuk programme.

TNB recorded an under-recovery of ICPT that amounted to RM3.50 billion for the first quarter this year (1Q22), up from RM3.21 billion in 4Q21. The group's

deposits, bank and cash balances as at end-March stood at RM4.67 billion, down from RM6.71 billion as at end-2021.

Nonetheless, Hong Leong Investment Bank analyst Daniel Wong and AmInvestment Bank analyst Gan Huey Ling view the government's latest announcement positively, as it signifies the government's commitment towards ICPT and incentive-based regulation (IBR) framework, allaying concerns that the framework would not be honoured.

"TNB will be able to recover an estimated RM7.8 billion through the surcharges and government's subsidies in 2H2022, which will significantly address its ballooning receivables and improve cash flow, as TNB needs to pay for the increasing fuel costs," said Hong Leong's Wong, who kept his 'buy' call on TNB with TP held at RM13.40.

AmInvestment's Gan also kept TNB on 'buy', with a fair value of RM12.00 per share.

According to *Bloomberg* data, TNB has been put on 'buy' by 10 research houses, while four have it on 'hold' and six have it on 'sell'; TPs for the stock range from RM6.60 to RM14.20.

TNB closed 19 sen or 2.3% lower at its intra-day low of RM8.00, giving it a market capitalisation of RM45.81 billion. The stock, which fell 13% this month alone, was trading at its lowest level in almost seven years.

