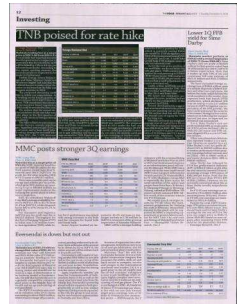


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TNB poised for rate hike

Tenaga Nasional Bhd
(Dec 2, RM9.89)

Maintain trading buy at a target price of RM11.86 from RM10.42:

A local daily had reported recently that the government is expected to announce that the electricity tariff will be hiked by 15% or 4.9 sen per kilowatt hour (kwh). According to the report, quoting sources, the announcement is expected to be made in Parliament.

Earlier, Energy, Green Technology and Water Minister Datuk Seri Maximus Ongkili had said that the Cabinet has yet to make a final decision on increase but the hike can happen anytime in 2014.

The proposed electricity tariff hike is within our expectations. At a briefing on the fourth quarter of financial year 2013 (4QFY13) in October, TNB mentioned that details of its incentive based regulation (IBR) could be revealed by year-end.

We reckon that the actual implementation of the rate hike may take place in the first quarter of 2014, with January being a strong possibility.

The hike is likely to encompass

certain factors, namely pipeline gas, liquefied natural gas (LNG), coal price and a base tariff hike. To recap, during the last tariff hike in May 2011, the 7.12% increase was broken down into 5.12% for the upward revision in gas price by RM3 per one million British thermal units (mmbTU) and 2% base tariff hike to account for inflationary pressures.

A tariff hike to account for the cut in gas subsidies will be earnings neutral for TNB. Pipeline gas is currently supplied to the power sector at RM13.70 per mmbTU vis-à-vis estimated market rates of RM45 per mmbTU. The proposal back in 2011 under the fuel cost pass-through mechanism (FCPT) was for a RM3 per mmbTU subsidy cut every six months until gas prices converge to market rates.

The tariff hike portion to account for LNG is positive for TNB, which is currently paying RM42 per mmbTU. TNB recognises one third of the incremental cost of LNG in its profit and loss. A tariff hike

would help TNB mitigate some of this incremental cost.

As for the coal price portion of the tariff hike, we do not think this will take place. TNB's current tariff applies to coal prices up to US\$85 (RM274) per tonne. With coal price currently at US\$82.80 per tonne, we reckon that a tariff adjustment for coal is not required.

Lastly, a base tariff hike would be earnings positive for TNB. The last two base tariff hikes took place in May 2011 and June 2006.

We leave our estimates unchanged for now, pending further clarity on the composition of the proposed tariff hike.

Recent developments suggest that structural reforms in the power sector are panning out as expected. We reckon that this will lower the overall cost of equity for TNB in the long run.

With this, we lower our weighted average cost of capital from 8% to 7.5% which raises our target price from RM10.42 to RM11.86. This implies FY14 and FY15 price-earnings ratio of 15.8 times and 13.5 times respectively. Maintain "trading buy". — *Alliance Research, Dec 2*

Tenaga Nasional Bhd					
FYE Dec 31 (RM mil)	2011	2012	2013	2014F	2015F
Revenue	32,241	35,848	37,131	38,750	40,309
Ebitda	5,879	8,986	10,277	10,775	11,778
Ebit	1,817	4,718	5,889	6,288	7,196
Pre-tax profit	1,351	6,073	5,253	5,647	6,605
Reported net profit	965	4,411	4,614	4,222	4,938
Core net profit	1,160	2,771	3,170	4,222	4,938
EPS (sen)	17.1	78.2	81.8	74.9	87.6
Core EPS (sen)	20.6	49.2	56.2	74.9	87.6
Alliance/Consensus (%)	-	-	76.8	97.9	107.7
Core EPS growth (%)	(54.4)	139.0	14.4	31.2	16.9
PER (x)	47.9	20.1	17.5	13.2	11.3
EV/Ebitda (x)	11.7	7.7	6.7	6.4	5.8
ROE (%)	3.6	7.7	9.0	10.1	10.9
Net gearing (%)	47.2	40.0	38.9	26.2	18.9
Net DPS (sen)	3.3	20.0	25.0	18.7	21.9
Net dividend yield (%)	0.3	2.0	2.5	1.9	2.2
BV/share (RM)	5.68	6.41	6.23	7.39	8.05
P/B (x)	1.7	1.5	1.6	1.3	1.2

Source: Alliance Research, Bloomberg