

PP14767/09/2012(030761)

Thursday, July 09, 2015

Tenaga Nasional Berhad

“Accepting 3B Project”

Latest Development

- Submit letter of acceptance.** TNB has announced that it had submitted the Letter of Acceptance (LOA) to the Energy Commission (EC) to takeover Project 3B plant from 1MDB. Subsequently, TNB had also entered in a share sale and purchase agreement (SSPA) with 1MDB to acquire a 70% stake owned by the latter in Jimah East Power Sdn Bhd (JEP) for cash consideration of RM46.98 million. JEP is the SPV to develop the 2x1000MW coal fired power plant (Project 3B); Mitsui & Co Ltd holds the remaining 30% of JEP.
- Key term.** The purchase price of RM46.98 million came as a surprise as 1MDB had previously said its actual cost incurred was RM83.68 million. In our view, the purchase price is fair given TNB’s stance of not paying premium price to 1MDB despite 1MDB already incurring start-up cost. Additionally, out of RM46.98 million of purchase price, 15% of it will be utilized for trust security for compliance by 1MDB of its warranties and undertakings pursuant to the SSPA.
- What now?** With the submission of LOA, TNB is now able to commission the project 3B plant development to meet the revised timeline of June 15, 2019 (Unit 1) and Dec 15, 2019 (Unit 2). The main hurdles of higher tariff of 26.67 sen has been cleared by EC to justify the higher cost of equipment associated with weakening Ringgit and higher interest cost.
- Gearing still acceptable.** The total cost of RM11.7 billion vs. RM11 billion original cost is expected to be financed through 80:20 debt to equity financing. However we believe TNB may keen to opt with notes issuance of up to RM10 billion as its annual

BUY (TP: RM15.20)

Current Price (RM)	RM12.48
New Fair Value (RM)	RM15.20
Previous Fair Value (RM)	RM15.20
Previous Recommend.	BUY
Upside To Fair Value	21%
Dividend Yield (FY15)	2.0%

Stock Code

Bloomberg	TNB MK
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Stock & Market Data

Listing	MAIN MARKET	
Sector	Power	
Shariah Compliance	Yes	
Issued Shares (mn)	5,643.6	
Market Cap (RM mn)	73,705	
YTD Chg In Share Price	-9.6%	
Beta (x)	1.0	
52-week Hi/Low (RM)	RM16.96	RM11.94
3M Average Volume (shrs)	13.0mn	
Estimated Free Float	38.79%	

Major Shareholders

Khazanah	29.6%
EPF	15.4%
ASB	8.7%

RM6 billion capex may not be able to cover the total cost. Should TNB proceed with notes issuance, TNB's gearing could potentially lift to 0.76x vs. 0.55x as at 2Q15.

- **Dividend payment still intact.** We understand TNB is keen to proceed with Track 3B by utilizing its internal generated funds to settle the RM46.98 million purchase prices. Based on this, we foresee that TNB's 30% dividend policy will largely be intact as several major projects have been completed. Its cash stood at a healthy level of RM4 billion as at 2Q15.
- **Increasing generation capacity.** The 2,000 MW will utilize coal as the main source of energy for electricity generation. This will enhance TNB generation capacity to 12,255 MW with a market share of 57.7% in 2020 from 50.2% currently in Peninsular Malaysia. With the completion of Track 3B, TNB will gradually shift its generation mix to 45% coal fired vs. 40% currently and slowly reducing the usage of expensive oil and distillates.
- **Buying Edra's 1MDB could shy investor away.** The news of TNB eyeing 1MDB's Edra Energy has shaken investors where TNB has lost market capitalization of RM2 billion for the past 2 months. Of note, Edra, which has some 15 power and desalination plants in five countries, with a book value of between RM16 billion and RM18 billion. Operationally, we feel that TNB may not be able to undertake all of Edra's assets despite Edra's steady revenue generation from its power plants. However, we feel that TNB may face a knee-jerk reaction from investors as various issues surrounding 1MDB could hurt the sentiments.
- **Investor should start accumulate TNB.** With the compensation amount now finally settled, we believe TNB's share price could recover. We hope that the heavy selling pressure could halt due to no advance payment involved and TNB only has to pay at a discount price as opposed to the previous rumour.
- **Impact to bottom line.** No impact to the bottom line at this stage as the project will only contribute to the financials in FY19 and hence we leave our forecast unchanged. However, we foresee the contribution from JEP could possibly surge TNB's bottomline by 3%-4% in FY19 as TNB has managed to acquire the higher tariffs awarded by EC.
- **Change to forecast.** We leave our forecast unchanged in FY15 as we expect TNB to delay its sukuk issuance to FY16. At the current environment, we foresee that TNB's sukuk issuance seems appealing due to dropping bond yields. The only downside is Ringgit weakening as it may put an upside risk to TB cost of borrowing. We feel that TNB should not delay any longer to revive Track 3B plant development as the delay could potentially disrupt Malaysia's reserve electricity margin (note: at 25% currently) and thus, this could hamper Malaysia's aspiration to become a high income nation by 2020. That said, we tweak our forecast in FY16 to incur the potential of 5%-6% finance cost from the sukuk issuance.

- **Valuation and recommendation.** We value TNB at RM15.20 and the stock is a **BUY**. TNB's share price will be driven by 1) the new mechanism namely FCPT and IBR 2) prolong weakness in coal price 3) steady electricity demand driven solid GDP growth this year of 5%.

Table 1: Peers Comparison

Company	Y/E Ended	Price (RM)	EPS (RM)		P/E (x)		P/B (x)		ROE (%)	TP	Call
			FY15	FY16	FY15	FY16	FY16	FY16			
MMC Corp	Dec	2.29	0.1	0.2	18.9	16.1	1.0	0.9	3.2	3.00	Buy
TNB	Aug	12.48	1.2	1.2	12.7	12.2	1.8	1.6	14.1	15.20	Buy
Gas Malaysia	Dec	2.51	0.1	0.1	25.0	20.6	3.3	3.2	17.0	2.89	Hold
Petronas Gas	Dec	21.08	0.9	0.9	25.0	24.3	4.0	3.7	21.4	23.20	Hold
Petronas Chemical	Dec	6.01	0.3	0.4	15.1	13.4	1.7	1.6	15.0	5.80	Hold
Malakoff	Dec	1.77	NA	NA	NA	NA	NA	NA	8.68	2.30	Buy
YTL Power	Dec	1.54	0.1	0.1	11.2	11.8	1.1	1.0	12.1	NA	NA
Average			0.5	0.6	19.4	17.3	2.3	2.2	13.8		

Source: Bloomberg, M&A Securities

Table 2: TNB Power Plant

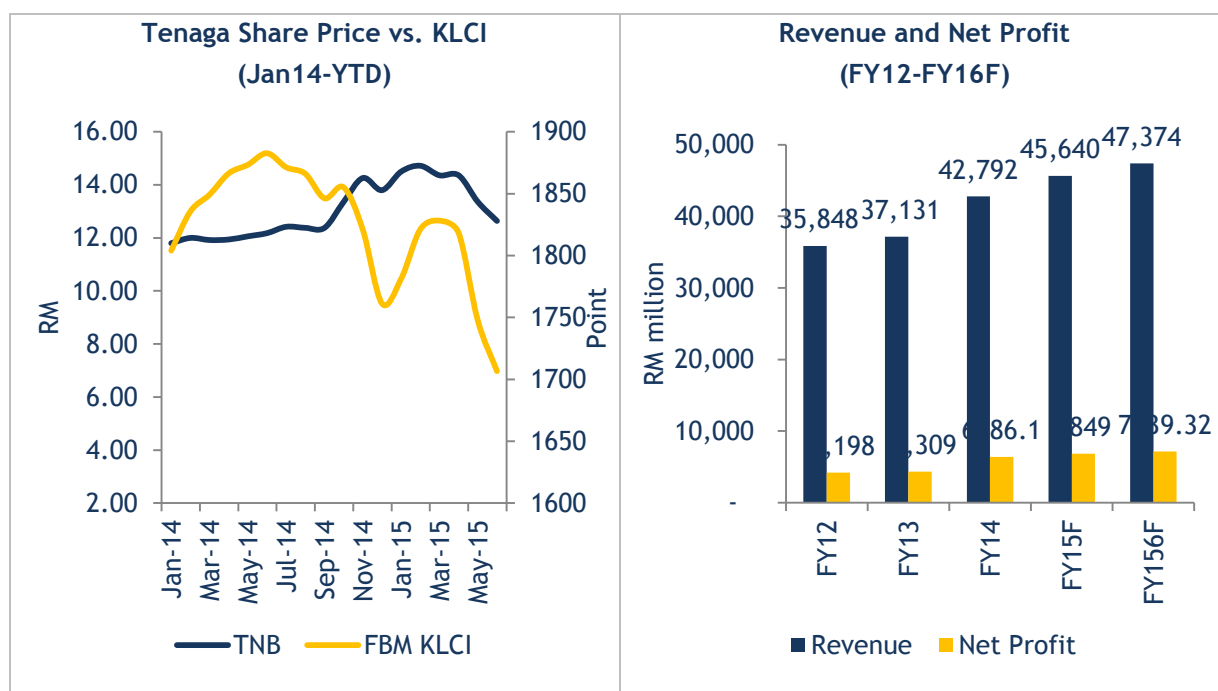
Plant	Company	Capacity (MW)	Type
Connaught Bridge Power Station	TNB	832	Combined cycle
Serdang	TNB	625	Gas Turbines
Sultan Iskandar, Pasir Gudang	TNB	729	Combined cycle
Sultan Ismail, Paka	TNB	1,139	Combined cycle
Tuanku Jaafar, Port Dickson	TNB	1,500	Combined cycle
Gelugor	TNB	758	Combined cycle
Sungai Perak Hydro Scheme	TNB	1,249	Hydro
Terengganu Hydro Scheme	TNB	400	Hydro
Cameron Hydro Scheme	TNB	262	Hydro
Cameron Highlands and Batang Padang Rehab	TNB	260	Hydro
Sabah	SESB	431	Thermal
Manjung	TNB	2,070	Coal
Sub-Total		10,255	
Jimah Track 3B	TNB	2,000	Coal
Total		12,255	

Source: TNB

Table 3: Financial Forecast

YE: Dec (RM million)	FY12	FY13	FY14	FY15F	FY16F
Revenue	35,848	37,132	42,792	45,640	47,374
EBITDA	9,385	9,057	12,053	14,200	14,484
Depreciation	-4,268	-4,570	-4,873	-5,653	-5,602
EBIT	5,117	4,487	7,181	8,547	8,882
Net Interest	-823	-711	-169	-550	-919
Result of associates	27	75	103	102	106
Exceptional items	0	1,683	0	-	0
PBT	5,537	5,534	7,114	8,099	8,068
Taxation	-1,331	-1,225	-688	-1,210	-1,239
Minority interest	-9	0	-40	-40	-40
PAT	4,198	4,309	6,386	6,849	6,789
EPS	58.1	82.8	114	112	111
EBITDA Margin	26.2%	24.4%	28.2%	31.1%	30.6%
PBT Margin	15.4%	14.9%	16.6%	17.7%	17.8%
PAT Margin	11.7%	11.6%	14.9%	15.0%	15.1%
PER (x)	8.47	10.5	11.56	13.5	12.6
P/BV (x)	1.1	1.4	1.7	1.7	1.6

Source: Bursa Malaysia, M&A Securities



Source: Bursa Malaysia, M&A Securities

M&A Securities

STOCK RECOMMENDATIONS

BUY	Share price is expected to be $\geq +10\%$ over the next 12 months.
TRADING BUY	Share price is expected to be $\geq +10\%$ within 3-months due to positive newsflow.
HOLD	Share price is expected to be between -10% and $+10\%$ over the next 12 months.
SELL	Share price is expected to be $\geq -10\%$ over the next 12 months.

SECTOR RECOMMENDATIONS

OVERWEIGHT	The sector is expected to outperform the FBM KLCI over the next 12 months.
NEUTRAL	The sector is expected to perform in line with the FBM KLCI over the next 12 months.
UNDERWEIGHT	The sector is expected to underperform the FBM KLCI over the next 12 months.

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