

Petronas Gas

2Q19 In Line

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2Q19 earnings, which rose 11% sequentially to RM507.7m, is well on track. However, the fear of tariff cut in the RP1, which takes effect next Jan, is the main reason for heavy selling pressure of late. However, with a 20% YTD contraction in share price, we believe the near-term negatives should have been priced in. As such, we keep our MP call with a revised target price of RM15.75/SoP share. The call is supported by decent yield of c.4%.

2Q19 matched expectations. 2Q19 core profit of RM507.7m came within expectation with 1H19 core income sliding 3% to RM965.5m making up 50%/52% of house/street's FY19 full-year estimates. It declared 2nd interim NDPS of 16.0 sen (ex-date: 13 Sep; payment date: 27 Sep) in 2Q19, the same amount paid in 1Q19 and 2Q18. This brings 1H19 NDPS to 32.0 sen which is the same payment in 1H18.

Sequential results led by GP and Utilities. 2Q19 core profit leapt 11% QoQ to RM507.7m although revenue only inched up slightly by 1%. This was largely due to: (i) stronger operating profit from Gas Processing (GP) by 11% or RM22m on lower depreciation as certain assets ended their useful life, (ii) 8% or RM15.0m higher Gas Transportation's (GT) earnings due to lower opex, and (iii) better Utilities earnings by 30% or RM13.8m on the back of better sales volume and prices. Meanwhile, RGT earnings were fairly flattish at RM158.5m while associate incomes rose 18% or RM7.1m to RM46.3m which we believe was due to better contribution from Kimanis IPP.

Tariff cut dented yearly earnings. On a YoY comparison, 2Q19 and 1H19 core profits fell slightly by 2% and 3% to RM507.7m and RM965.5m, respectively, primarily due to tariff rates cut for GT and RGT Pengerang for the Pilot Regulatory Period in 2019. As such, operating profit for both segments declined 19% and 10% in 2Q19, and 21% and 10% in 1H19, respectively. Nonetheless, GP posted stronger earnings by 27% in 1Q19 and by 24% and 1H19 owing to the above-mentioned lower depreciation charges and higher revenue while Utilities also registered solid earnings, higher by 47% and 21% on better volume and prices.

TPA remains the only issue going forward. Although the Pilot Period of 2019 will see less severe impact to PETGAS, its earnings will be impacted by two step-downs; in Regulatory Period 1 (RP1) in 2020-2022 and Regulatory Period 2 (RP2) in 2023-2025, before stabilising from 2026 onwards. We take the view that its ROA will eventually taper to 8% by 2026. Hence, we expect base-tariff for PGU to reduce sharply by 60% to RM0.502/GJ in 2026 from RM1.248/GJ in 2018. As such, this will continue to dent sentiment on PETGAS. In all, we keep our FY19-FY20 estimates unchanged where we have factored in a base-tariff cut in 2020 as mentioned above.

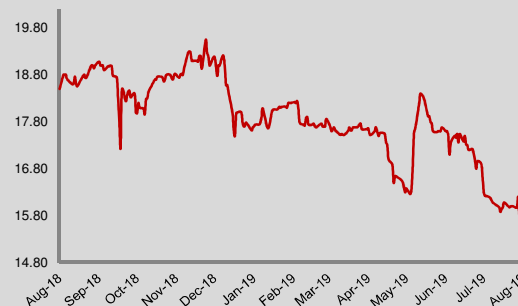
Sell-down should have reflected negatives; keep MP. PETGAS continued to face heavy sell down in recent weeks with share price falling 20% YTD which we believe should have priced in near-term negatives, especially for the RP1 tariff cut. To reflect its latest risk profile, we adjusted WACC to 6.6% from 6.4% for core gas business as well as target price for GASMSIA (MP; TP: RM3.00) that reduced our SoP-driven target price to RM15.75 from RM16.55, implying FY20E PER of 19.2x which is at -0.5SD 3-year mean. Thus, we keep our MARKET PERFORM call unchanged, which is supported by a decent yield of c.4%.

Upside risk to our call is higher-than-expected return on regulated asset base.

MARKET PERFORM ↔

Price : **RM15.36**
Target Price : **RM15.75** ↓

Share Price Performance



KLCI	1,590.84
YTD KLCI chg	-5.9%
YTD stock price chg	-20.0%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	PTG MK
Market Cap (RM m)	30,393.3
Shares Outstanding	1,978.7
52-week range (H)	20.00
52-week range (L)	14.74
3-mth avg daily vol:	689,186
Free Float	26%
Beta	1.0

Major Shareholders

Petroleum Nasional Bhd	60.7%
Employees Provident Fund	9.3%
Kumpulan Wang Persaraan	4.4%

Summary Earnings Table

FY Dec (RM m)	2018A	2019E	2020E
Turnover	5498	5760	5659
EBIT	2570	2559	2160
PBT	2352	2526	2155
Net Profit (NP)	1810	1930	1646
Core Net Profit	1826	1930	1646
Consensus (NP)		1850	1802
Earnings Revision (%)		-	-
Core EPS (sen)	92.3	97.5	83.2
CNP growth (%)	2.9	5.7	-14.7
NDPS (sen)	72.0	68.3	58.2
BV/Share (RM)	6.56	6.91	7.16
NTA/Share (RM)	6.56	6.91	7.16
Core PER	20.8	15.7	18.5
PBV (x)	2.93	2.22	2.14
Price/NTA (x)	2.93	2.14	2.07
Gearing (%)	N Cash	N Cash	N Cash
Dividend Yield (%)	4.7	4.4	3.8

28 August 2019

Income Statement								
FY Dec (RM m)	2Q FY19	1Q FY19	Q-o-Q Chg	2Q FY18	Y-o-Y Chg	1H FY19	1H FY18	Y-o-Y Chg
Turnover	1380.2	1367.6	1%	1358.3	2%	2747.8	2709.0	1%
EBITDA	935.5	968.5	-3%	936.8	0%	1904.0	1869.1	2%
Depreciation	(274.0)	(277.4)	-1%	(278.6)	-2%	(551.4)	(552.0)	0%
EBIT	661.5	691.1	-4%	658.2	1%	1352.6	1317.1	3%
Interest expense	(56.5)	(60.3)	-6%	(41.9)	35%	(116.8)	(80.9)	44%
Associates	46.3	39.2	18%	16.5	180%	85.6	33.6	155%
Exceptional items	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
Pretax profit	651.3	670.0	-3%	632.8	3%	1321.3	1269.8	4%
Taxation	(136.5)	(139.3)	-2%	(95.8)	42%	(275.7)	(227.4)	21%
Profit after tax	514.8	530.8	-3%	537.1	-4%	1045.6	1042.4	0%
Minority interest	(11.9)	(15.3)	-22%	(27.8)	-57%	(27.2)	(49.9)	-45%
Net profit	502.9	515.5	-2%	509.3	-1%	1018.4	992.5	3%
Core net profit	507.7	457.8	11%	516.1	-2%	965.5	992.8	-3%
EPS (sen)	25.7	23.1	11%	26.1	-2%	48.8	50.2	-3%
DPS (sen)	16.0	16.0	0%	16.0	0%	32.0	32.0	0%
NTA/share (RM)	6.65	6.56	1%	6.49	3%	6.65	6.49	3%
EBITDA margin	68%	71%		69%		69%	69%	
EBIT margin	48%	51%		48%		49%	49%	
Pretax margin	47%	49%		47%		48%	47%	
Effective tax rate	21%	21%		15%		21%	18%	

Source: Company

Segmental Breakdown								
FY Dec (RM m)	2Q FY19	1Q FY19	Q-o-Q Chg	2Q FY18	Y-o-Y Chg	1H FY19	1H FY18	Y-o-Y Chg
Turnover								
Gas Processing	427.1	424.1	1%	395.2	8%	851.2	789.0	8%
Gas Transportation	292.9	289.7	1%	344.2	-15%	582.6	677.9	-14%
Utilities	352.4	351.5	0%	308.3	14%	703.8	631.9	11%
RGT	307.9	302.3	2%	310.6	-1%	610.2	610.2	0%
Others	0.0	0.0	0%	0.0	0%	0.0	0.0	0%
Group Turnover	1380.2	1367.6	1%	1358.3	2%	2747.8	2709.0	1%
Segment Results								
Gas Processing	217.7	195.7	11%	171.2	27%	413.4	332.5	24%
Gas Transportation	215.0	200.0	8%	265.6	-19%	415.1	525.6	-21%
Utilities	59.3	45.5	30%	40.4	47%	104.8	86.3	21%
RGT	158.5	157.7	0%	177.0	-10%	316.2	351.0	-10%
Others	11.0	92.1	-88%	4.0	175%	103.1	21.6	376%
Group PBT	661.5	691.1	-4%	658.2	1%	1352.6	1317.1	3%
PBT Margin								
Gas Processing	51%	46%		43%		49%	42%	
Gas Transportation	73%	69%		77%		71%	78%	
Utilities	17%	13%		13%		15%	14%	
RGT	51%	52%		57%		52%	58%	
Others	N/A	N/A		N/A		N/A	N/A	
Group PBT Margin	48%	51%		48%		49%	49%	

Source: Company

28 August 2019

Valuation - New				
(RM m)	Equity value	RM/Share	%	Valuation Basic
Gas Business	23,720.6	11.99	76.2%	DCF @ 6.6% WACC, g = 2%
Melaka RGT	2,124.6	1.07	6.8%	DCF @ 8.1% WACC
Kimanis IPP	838.2	0.42	2.7%	DCF @ 4.0% WACC
Pengerang RGT	2,077.9	1.05	6.7%	DCF @ 6.0% WACC
Gas Malaysia	554.1	0.28	1.8%	TP: RM3.00 @ 14.8% equity stake
Net Cash/(Debt)	1,800.8	0.91	5.8%	Adjusted FY20E at group's level
	31,116.2	15.73	100.0%	
No of shares	1,978.7			
SOP per shares	RM15.75			Round up to the nearest RM0.05

Source: Kenanga Research

Valuation - Old				
(RM m)	Equity value	RM/Share	%	Valuation Basic
Gas Business	25,196.4	12.73	76.9%	DCF @ 6.4% WACC, g = 2%
Melaka RGT	2,256.5	1.14	6.9%	DCF @ 8.1% WACC
Kimanis IPP	855.6	0.43	2.6%	DCF @ 4.0% WACC
Pengerang RGT	2,098.8	1.06	6.4%	DCF @ 6.0% WACC
Gas Malaysia	563.3	0.28	1.7%	TP: RM3.05 @ 14.8% equity stake
Net Cash/(Debt)	1,800.8	0.91	5.5%	Adjusted FY20E at group's level
	32,771.5	16.56	100.0%	
No of shares	1,978.7			
SOP per shares	RM16.55			Round up to the nearest RM0.05

Source: Kenanga Research

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Peer Comparison

Name	Last Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target	Rating
	(RM)				Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.		
GAS MALAYSIA BHD	2.85	3,659.4	Y	12/2019	2.9%	7.7%	8.2%	2.2%	21.5	19.9	19.5	3.6	3.3	17.3%	4.5%	3.00	MP
MALAKOFF CORP BHD	0.870	4,251.7	Y	12/2019	-0.3%	-0.1%	10.5%	4.5%	19.8	17.9	17.2	0.8	0.8	4.3%	4.5%	1.00	OP
PESTECH INTERNATIONAL BHD	1.43	1,092.9	Y	06/2020	17.3%	10.5%	25.8%	13.5%	15.1	12.0	10.6	2.4	2.0	18.3%	0.0%	1.75	OP
PETRONAS GAS BHD	15.36	30,393.3	Y	12/2019	4.8%	-1.8%	5.7%	-14.7%	16.6	15.7	18.5	2.3	2.2	14.5%	4.4%	15.75	MP
TENAGA NASIONAL BHD	13.60	77,341.7	Y	12/2019	3.2%	1.8%	2.6%	2.0%	14.2	13.8	13.5	1.3	1.3	9.3%	3.6%	13.40	MP
YTL POWER INTERNATIONAL BHD	0.695	5,334.3	N	06/2019	3.4%	2.6%	-1.6%	8.0%	8.0	8.1	7.5	0.4	0.4	4.6%	7.2%	0.880	MP
Simple Average					5.2%	3.5%	8.5%	2.6%	15.9	14.6	14.5	1.8	1.7	11.4%	4.0%		

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

- OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
- MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
- UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

- OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
- NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
- UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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