Utilities

NEUTRAL

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Life After Data Centre Exuberance

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We remain NEUTRAL on the sector. We believe justice has been done, for instance, to TENAGA (MP; TP: RM14.50) with a 40% appreciation in its share price YTD which has added RM23b to its market capitalisation on the back of the frenzy on data centre-related stocks. Nonetheless, we will still hold utilities stocks for their earnings defensiveness backed by regulated assets and a decent dividend yield of 3% to 6%. TENAGA guided for electricity demand growth of 2.5% to 3.0% in FY24, driven by electricity demand from new data centres. Meanwhile, stabilising coal prices meant that negative fuel margin, which blew a big hole in power producers' earnings in CY23, is unlikely to recur in CY24, while normalising gas prices will have a mixed impact on gas utilities.

New data centres drive electricity demand growth. TENAGA guided for a decent electricity demand growth of 2.5% to 3.0% in Peninsular Malaysia in FY24 (from a high base of 3.6% in FY23 on economy reopening) underpinned by data centres completed in FY23 (c.635MW) and nine more (c.700MW) to be completed this year, with two of them (535W) already completed in 1QFY24. Over a longer time horizon, **TENAGA** projects a total potential demand of >5,000MW of electricity annually from new data centres by CY35. While **TENAGA** is a good proxy to the energy-intensive new data centres, we believe justice has been done with a 40% appreciation in its share price YTD, adding RM23b to its market capitalisation.

TENAGA in significant capex programs. TENAGA is also embarking on the transition to green energy with a pipeline of green energy projects with a combined capacity of c.7,300MW comprising hydro plants, hybrid hydro-floating solar PV projects, a hydrogen-ready combined cycle power plant, corporate green power program (CGPP) and large-scale solar parks. In FY24, its energy transition capex is budgeted at RM3.2b. Meanwhile, it also needs to upgrade the transmission and distribution (T&D) system including power grid to meet the demand from the growing renewable energy (RE) assets. A higher T&D capex will increase **TENAGA**'s regulated asset base (RAB), resulting in higher absolute earnings based on a return pegged to WACC of 7.3% under the Regulatory Period 3 (RP3). **TENAGA** has set aside RM7b capex in FY24 for its regulated business and RM5b to RM6b for non-regulated power generation business such as solar farms and hydropower plants.

Stable fuel prices. Meanwhile, prices for coal and gas have been fairly benign in the past six months as opposed to a surge in 2HCY22, followed by a collapse in 1HCY23. As a result, **TENAGA's** receivables, including Imbalance Cost Pass-through (ICPT) receivables declined by a sharp 54% to RM10.2b in 1QFY24 from a peak of RM22.0b in 4QFY22. The shrinking ICPT receivables will result in lower working capital requirements and hence lower interest expenses and better earnings going forward for **TENAGA.** On the other hand, stabilising coal prices mean that negative fuel margin that blew a hole in power producers' earnings in CY23 is unlikely to recur in CY24. **TENAGA** reported a smaller negative fuel margin of RM25.8m in 1QFY24 against a whopping RM618.7m in FY23 while **MALAKOF (MP; TP: RM0.68)** posted negative fuel margin of RM37.2m in 1QFY24 as opposed to a massive RM828.2m registered in FY23.

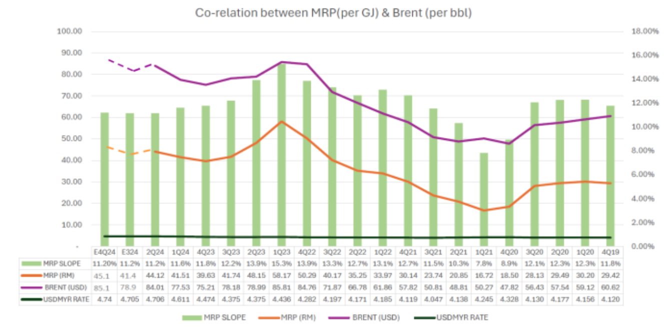
Mixed impact on gas utilities. While the movement of gas prices has neutral earnings impact in the long run under the regulated framework, soft gas price is positive on **PETGAS (MP; TP: RM17.87)** over the short term as it translates to lower internal gas consumption (input cost) for its regulated business as well as non-regulated utilities segment. The utilities segment uses gas as fuel to generate and supply power, stream and industrial gasses to industries. However, weak gas price works against **GASMSIA's (MP; TP: RM3.59)** non-regulated retail margins, which are calculated based on a fixed percentage on the gas selling price. Nonetheless, this will be cushioned by gas sales volume growth of 4% to 5% in FY24, driven largely by strong demand from the rubber glove, consumer product and F&B sectors.

We remain NEUTRAL on the sector. The sector offers earnings defensiveness backed by regulated assets. We downgrade **TENAGA** to **MARKET PERFORM** from **OUTPERFORM** following its recent run-up in its share price. Other utilities stocks are fully valued as well. Nonetheless, utilities stocks still offer dividend yields of 3% to 6%. We have no top pick for the sector.

Indonesia Coal Benchmark Price (USD)

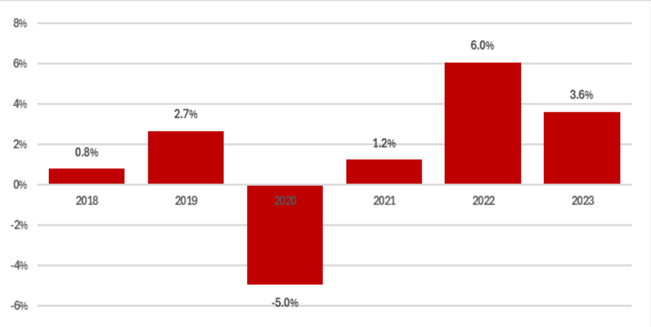
Source: Bloomberg

Natural Gas Price Movement



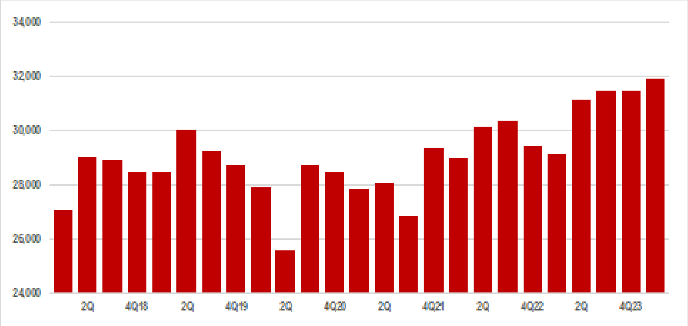
Source: GASMSIA

TENAGA: Annual Electricity Demand Growth



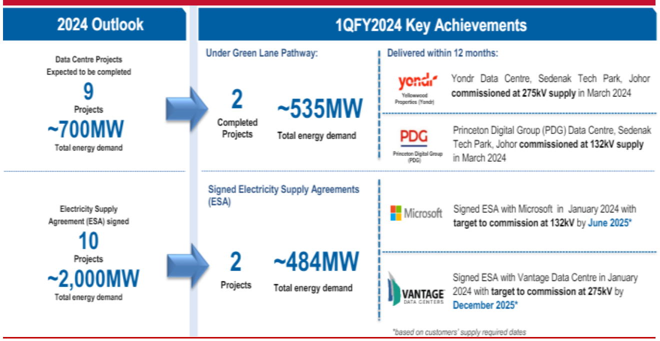
Source: Tenaga

TENAGA: Monthly Electricity Sales (GWh)



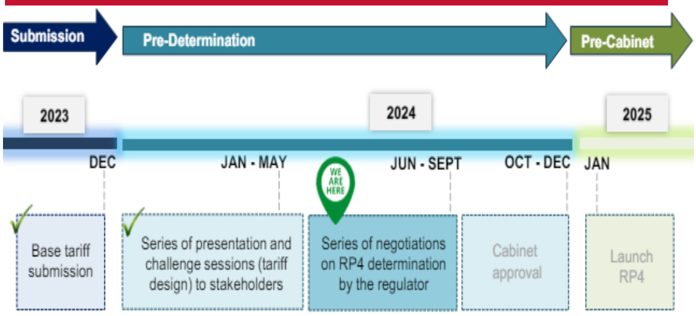
Source: Tenaga

Data Centre Prospects



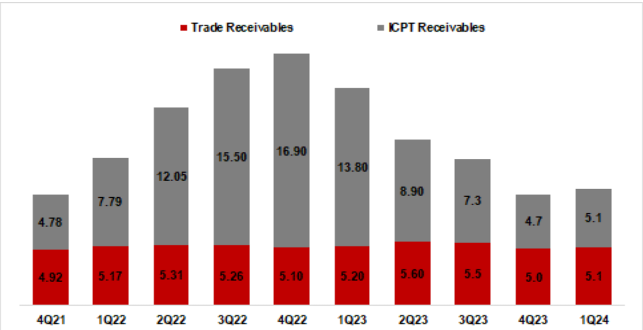
Source: Tenaga

TENAGA: RP4 Milestone



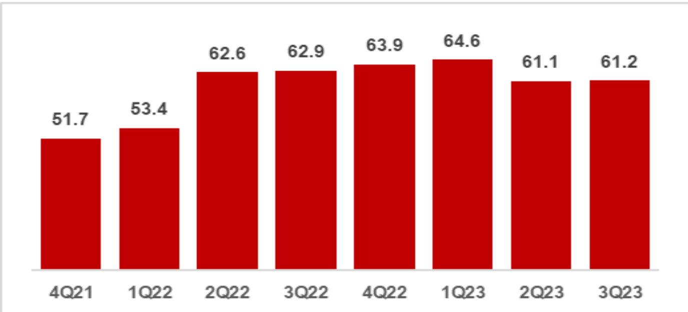
Source: Tenaga

TENAGA: Trade & Other Receivables (RM b)



Source: Tenaga

TENAGA: Borrowings (RM b)



Source: Tenaga

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net. Div. (sen)	Net Div Yld
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
GAS MALAYSIA BHD	MP	3.60	3.59	-0.3%	4,622.4	Y	12/2024	28.4	27.5	-4.9%	-3.0%	12.7	13.1	3.2	25.8%	22.7	6.3%
MALAKOFF CORP BHD	MP	0.775	0.680	-12.3%	3,787.4	Y	12/2024	4.7	5.8	-71.9%	24.1%	16.5	13.3	0.9	5.2%	3.8	4.9%
PETRONAS GAS BHD	MP	18.34	17.87	-2.6%	36,289.9	Y	12/2024	98.4	100.7	5.2%	2.4%	18.6	18.2	2.6	14.2%	72.0	3.9%
SAMAIDEN GROUP BHD	OP	1.29	1.51	17.1%	539.9	Y	06/2024	3.5	5.3	26.4%	51.9%	37.1	24.4	5.2	14.9%	0.0	0.0%
SOLARVEST HOLDINGS BHD	OP	1.56	1.91	22.4%	1,084.8	Y	03/2025	6.8	8.5	62.5%	24.2%	22.8	18.3	3.9	19.5%	0.0	0.0%
TENAGA NASIONAL BHD	MP	13.72	14.50	5.7%	79,402.2	Y	12/2024	75.2	81.9	40.1%	8.9%	18.3	16.8	1.3	7.1%	37.2	2.7%
Sector Aggregate					**165,720.0**					**55.8%**	**3.8%**	**16.4**	**15.8**	**2.7**	**15.0%**		**2.7%**

Source: 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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