



Power utilities still a good defensive sector

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KUCHING: Analysts peg power utilities as a good defensive sector under these uncertain times, especially when valuations have become less expensive following the recent sell-down.

This comes as the second Imbalance Cost Pass-Through (ICPT) surcharge in the first half of 2019 (1H19), which reaffirmed government's commitment to the ICPT mechanism, offers earnings certainty to Tenaga Nasional Bhd, which is a positive for sentiment.

"Government's commitment on the ICPT mechanism is key. The continued ICPT surcharge of 2.15 sen/kWh in 1H19 is not unexpected given the rising coal prices," opined Kenanga Investment Bank Bhd's research arm (Kenanga Research).

"The applicable coal prices in 3Q18 and 4Q18 were RM359.87 per metric tonne (MT) and RM428.42 per MT, respectively, which were much higher than the benchmark coal price of RM315.9 per MT for new Regulatory Period 2 (RP2) in 2018-2020.

"Thus, the additional generation cost in the second half of 2018 was RM1.82 billion. The RM2.15 sen per kWh surcharge reaffirmed the government's commitment



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Kenanga Research saw that the independent power producers (IPPs) experienced a roller-coaster ride in their share prices for the past six months.

This is especially so for YTL Power Bhd (YTL Power), which saw a strong rebound from the all-time-low of RM0.75 in end-May to a high of RM1.27 in July, thanks to bargain hunting. It now trades around its six-month low at RM0.80-level.

"We believe it is trading fairly

at the current level given the lack of immediate earnings catalyst after the capacity payment cut on Paka's PPA Extension before the two offshore greenfield power plants come into system in three to four years' time.

Meanwhile, Malakoff Corporation Bhd (Malakoff) also saw a new low of RM0.825 in end-June before bargain hunting pushed the IPP to the recent high of RM1.05 in early August 2018.

Kenanga Research saw that Malakoff experienced selling pressure coming in after the announcement of Alam Flora Sdn

Bhd's acquisition in early-August 2018 and the stock is now trading at a six-month low of around RM0.80-level.

"Although it is a related-party transaction, we are fairly positive as it gives well with the group's long-term aspiration in renewable energy and is a long-awaited earning catalyst. Besides, the acquisition is fairly priced," it opined.

"Nonetheless, we still see value in Malakoff as the heavy sell-down in the past 20 months has more than priced in foreseeable negatives."

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Kenanga Research

On the other hand, the research firm was pleased to see that Pestech International Bhd (Pestech) finally securing the long-awaited Gemas-Johor Bahru Double Track electrification project, which is worth a total of RM474 million for two packages.

This was a much-needed catalyst for Pestech whose share price has been lacklustre in the past two years despite a commendable earnings record, it said.

Meanwhile, the recent 3Q18 results season was another disappointment with Tenaga's 3Q18, YTL Power's 1Q19 and Malakoff's 3Q18 missing expectations.

To note, Tenaga's 3Q18 results missed forecast on higher fuel costs as well as rising finance costs on new sukuk issuance. YTL Power's 1Q19 earnings fell short of expectations led by PowerSeraya's losses for the first time while narrowing losses at YES was the only positive.

Malakoff's 3Q18 results were hit by another boiler-related issue in TBE, which may lead to operational uncertainties.

Pestech had a slow start in FY19 in the seasonally weak 1Q19 due to lower work claim progress.

Going forth, Tenaga should see better earnings in 1H19 as the higher fuel costs in 2H18 will be adjusted by the abovementioned surcharge in 1H19 while YTL Power expects a full-year contribution in FY19 from Paka Power Plant, which recommenced in September 2017 after it resolved a dispute with Tenaga pertaining to a land issue.

However, YTL Power's dividend pay-out could be lower as it needs to conserve cash for two greenfield projects, namely PT Tanjung Jati coal-fired power plant in Indonesia and Attarat Power's oil shale-fired power plant in Jordan over the next three to four years.

Meanwhile, Malakoff's earnings are likely to be flattish given that upside is capped by cut in its SEV Power Plant's capacity payment following the PPA Extension Contract. Elsewhere, Pestech should see earnings growth on the back of its RM2 billion order-book coupled with new contract flows to sustain earnings momentum.



04 Jan 2019
Borneo Post (Kuching), Malaysia

Author: Ronnie Teo • Section: Business • Page: B2 • Printed size: 548.00cm²
Region: KL • Market: Malaysia • Photo: Full Color • Item ID: MY0034750539

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SUMMARIES

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