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Aussie coal supply disruption impacts TNB

While steel players stay resilient, they will not be immune to pending electricity tariff review

by **Melody Song**
FD@bizedge.com

KUALA LUMPUR: The severe flooding in Australia has resulted in a dip in Tenaga Nasional Bhd's (TNB) share price on the back of rising coal prices following a supply disruption, although this could represent an opportunity to accumulate shares in the national utility company, say some analysts.

TNB's share price has come under pressure since several towns in the state of Queensland were put on flood alert following a Boxing Day deluge. The stock ended five sen lower to RM6.67 yesterday with 16.65 million shares traded. Despite the continued rally of the FBM KLCI, TNB's stock has lost 5.2% from its recent high of RM7.03 on Dec 9.

Queensland and New South Wales are Australia's top producers of high-rank black coal used in metallurgical processes and power generation. Steam coal, also known as thermal coal, is used in power generation, while coking coal is used in the production of iron and steel.

In its financial year ended Aug 31 (FY10), TNB purchased about 17% of its coal from Australia, 71% from Indonesia and 11% from South America.

OSK Research in a recent note said despite TNB being dragged down by rising coal prices due to the La Nina effect, its fundamentals remained intact. "We believe TNB's fundamentals still justify a buy for those with a longer term investment horizon," it said.

In contrast, the possible tightening of coal supply is yet to be reflected in the share prices of most local steel players. In fact, several players, including Malaysia Steel Works (KL) Bhd (Masteel), Lion Industries Bhd and Ann Joo Resources Bhd, saw their share prices rising during the same period.

A local analyst told *The Edge Financial Daily* that among the local steel players, only Ann Joo would require coking coal to fuel its blast furnace, for which commissioning is expected to be delayed until the end of this quarter.

"I don't know whether Ann Joo has yet to stock up on coking coal or has already done so, but eventually everyone is going to be affected by rising costs," he said, adding that despite the present high prices, millers have not been able to react immediately.

He said most steel players would require electricity to power their steel plants. Hence they would not be immune to TNB's pending tariff review, which in turn would be affected to a certain extent by the increase in coal prices especially if the mines are shut for an extended period.

> "TNB's tariffs are reviewed bi-annually in January and July with coal costs being a key component in adjusting the rates."

Meanwhile, China-based metallurgical coke producer Sino Hua-An International Bhd has also seen its share price rise from about 34 sen to 36 sen since late December, despite RHB Research's Dec 27 underperform call on the counter with a target price of 33 sen.

Sino Hua-An produces coking coal exclusively for the China market and does not expect the situation in Australia to have any significant impact on the company as it buys and sells locally, a company official told *The Edge Financial Daily*.

It is estimated that nearly half of the world's coking coal for Asia's steel mills comes from Queensland. The floods have forced 75% of its coal mines to close, said the state's premier Anna Bligh yesterday. According to *Reuters*, Queensland's ports have an annual coal export capacity of 225 million tonnes.

In a knee-jerk reaction to the limited supply, analysts are expecting spot prices to rise to levels seen in 2008, when floods in the state caused coking coal prices to jump to more than US$300 (RM921) a tonne from US$125.

According to *Reuters*, spot prices for coking coal have risen 10% in a month to about US$250 a tonne, with some analysts expecting the mines to be shut for up to three months.

With regard to the use of thermal coal, it is understood that coal-fired power accounts for about 40% of electricity generation in Malaysia.

For TNB, the costs of coal in FY10 accounted for 48% of its fuel expenses based on a full-year average cost of US$88.20 per tonne.

Local brokerage firm AmResearch said Newcastle coal spot prices have risen by 18% over the past month to US$126 per tonne currently, which is 26% above its FY11F-FY13F coal assumption of US$100 per tonne.

"Based on current coal prices and US$ to RM exchange rate, we estimate that TNB's FY11F-FY13F net profits could drop by 28%-29%," it said. "But TNB's tariffs are reviewed bi-annually in January and July with coal costs being a key component in adjusting the rates."

It added that for now, it maintained its forecasts pending further guidance on TNB's coal costs and that it believed the spike in coal prices were also affected by the unusually cold weather in Europe and the US.

AmResearch has a hold call on TNB, with an unchanged target price of RM7.20 following its 1-for-4 bonus issue which went ex last week.

Sino Hua-An produces metallurgical coke

IN the article that appeared in *The Edge Financial Daily* yesterday titled "Aussie coal supply disruption impacts TNB", we would like to clarify that Sino Hua-An produces metallurgical coke exclusively for the China market, and buys coking coal and sells metallurgical coke locally.