Deutsche Bank

20 September 2004

YTL Power

Reuters: **YTLP.KL** Bloomberg: **YTLP MK** Exchange: **KLSE** Ticker: **YTLP.KL**

Growth story gradually crystallising; upgrade to Buy

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Rating Upgrade

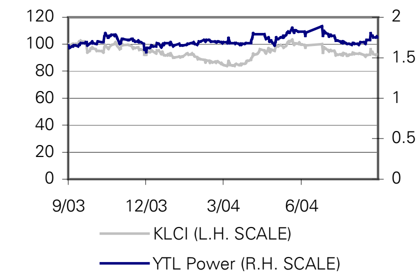
Buy

Price at 15 September 2004 (RM)	**1.75**
Price target - 12mth (RM)	**2.24 (+28.0%)**
52-week range (RM)	**1.90 - 1.55**
Previous rating	**Hold**
KLCI	**853.24**

Key changes

Price target (chg)	1.85 to 2.24 ↑	**21%**
Sales (FYE chg)	3,118 to 3,364 ↑	**8%**
Op prof margin (FYE chg)	39.1 to 41.6 ↑	**3%**
Net profit (FYE chg)	638 to 682 ↑	**7%**

Price/price relative



Performance (%)	1m	3m	12m
Absolute	*4.8%*	*-3.8%*	*6.7%*
KLCI	*4.6%*	*5.3%*	*14.8%*

Stock data

Market cap (RMm)	**8,210.1**
Market cap (US$m)	**2,160.8**
Shares outstanding (m)	**4,691.5**
Avg daily volume (US$m)	**0.77**
Major Shareholders: YTL Corp	**61%**
Free float	**30.0%**
Beta (2 years)	**0.57**
Est. 3 year EPS growth	**1.9%**

Financial data	FYE
ROE	**13.2%**
ROA	**3.3%**
Net debt/equity	**134.4%**
Book value/share (RM)	**1.06**
Price/book	**1.7x**
Net interest cover	**3.1x**
Operating profit margin	**41.5%**

Comparatives

Malakoff (MLKF.KL), RM6.30			Buy
	2003A	2004F	2005F
P/E (x)	8.0	12.2	10.2
EV/EBITDA (x)	4.7	6.9	8.3
Price/book (x)	1.50	1.79	1.59
Tenaga (TENA.KL), RM11.00			**Buy**
	2003A	2004F	2005F
P/E (x)	23.9	24.6	19.3
EV/EBITDA (x)	10.9	11.5	10.0
Price/book (x)	1.86	2.22	2.03

Upcoming events	Date
1Q05 Results	29 Nov 2004

Related recent research	Date
YTLP: 1H Results maintain Hold Niklas Olausson, CFA	15 Mar 2004

Foundation for positive long-term performance; upgrading to Buy

Armed with RM4bn gross cash, a strategy to re-invest, broadening expertise and good timing, YTLP has the foundation for a long-term rerating. It is also emerging as a Malaysian water concept stock. Recent newsflow has been positive, especially on the UK water front. We have raised our valuation by 21% to RM2.24 and our call from Hold to Buy.

UK/US road show: positive newsflow

YTLP continues to look for investments to re-deploy its RM4bn war chest. We believe that Jawa Power being purchased at 4x PER, is only the start in Indonesia. There is also potential for YTLP to participate in Malaysia's water sector restructuring further out. Meanwhile, Wessex got a favourable draft tariff review with an average 4.2% real price increase.

EPS and target upgraded; upside bias to ROEs

We have upgraded basic EPS by 5-26% and the DCF/RAB-driven target from RM1.85 to RM2.24 as we raise the Wessex valuation (in line with DB UK's methodology) and include the 35% stake in Jawa Power. There is zero assumed for additional power sales or 'option value' on its cash pile. The latter is conservative given an expanding opportunity pool.

Yield (4%) and growth; attractive long-term investment

The 'EB' overhang is likely to remain in the near term, but a valuation gap has opened. YTLP has underperformed the UK water sector by around 15% in 2004 as the recent favourable water review has not been priced in locally. Ratings are undemanding at 11.8x FD FY06F EPS and low-risk 4% yield. Risks include rising bond yields, FX volatility and PPA re-negotiation.

Forecasts and ratios

Year End Jun 30	2003A	**2004A**	2005F	2006F	2007F
Sales (RMm)	2,999.5	**3,203.7**	3,364.0	3,694.9	3,829.9
EBITDA (RMm)	1,613.3	**1,862.8**	1,942.1	2,147.6	2,215.2
Net profit (RMm)	476.37	**613.46**	682.32	801.26	847.20
EPS consensus (RM)	NA	**0.13**	0.14	0.15	NA
EPS New (RM)	0.11	**0.14**	0.15	0.18	0.19
EPS Old (RM)	0.13	**0.14**	0.14	0.14	0.19
Chg to previous EPS	*-21.1%*	***-1.8%***	*5.4%*	*25.7%*	NA
EPS growth	*3.0%*	***30.9%***	*9.7%*	*17.4%*	*5.7%*
PER (x)	13.27	**12.18**	11.58	9.86	9.32
EV/EBITDA (x)	7.84	**7.96**	8.73	7.85	7.54
DPS (net) (RM)	0.07	**0.07**	0.07	0.07	0.07
Yield (net)	*5.2%*	***4.3%***	*4.0%*	*4.0%*	*4.0%*

Source: Deutsche Bank AG estimates, Company data

[1]Pre-exceptionals/extraordinaries, EPS above is BASIC and does not include dilution from warrants, exchangeable bonds and ESOS
[2]Multiples and yields calculations use average historical prices for past years and spot prices for current and future years, except P/B which uses the year end close.

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Investors should consider this report as only a single factor in making their investment decision.

DISCLOSURES AND ANALYST CERTIFICATIONS ARE LOCATED IN APPENDIX 1

Model updated: 16 September 2004

Equity Research

Asia

Malaysia

Power/Utilities

YTL Power

Reuters code YTLP.KL

Buy

Price as at 16-Sep	RM1.76
Target Price	RM2.24

Company Website
http://http://www.ytl.com.my

Company description

YTL Power International Berhad is an investment holding company which provides administrative and technical support services. Through its subsidiaries, the Company develops, constructs, maintains, and operates power stations which includes Paka Power Station in Terengganu and Pasir Gudang Power Station in Johor.

Research Team

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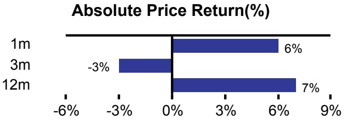
Absolute Price Return(%)



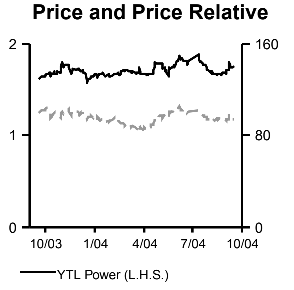
52-week Range:	RM1.55 - RM1.90
Market Cap (m):	RM 8,257
	US$ 2,173

Company identifiers

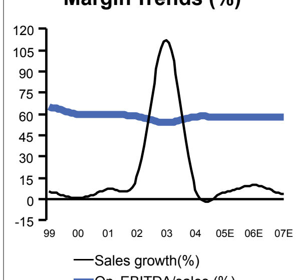
Bloomberg	YTLP MK
Cusip	NA
SEDOL	B01GQS6

Y/E 30 June	1999	2000	2001	2002	2003	2004	2005E	2006E	2007E
SUMMARY									
Headline EPS (RM)	0.13	0.08	0.10	0.10	0.11	0.14	0.15	0.18	0.19
P/E ratio Headline (x)	9.1	18.3	13.5	12.5	13.3	12.2	11.6	9.9	9.4
Headline EPS growth (%)	40.9	-36.0	15.8	6.0	3.0	30.9	9.7	17.4	5.7
EPS FD (RM)	0.13	0.08	0.10	0.11	0.10	0.14	0.13	0.15	0.16
P/E ratio FD (x)	9.0	18.2	13.3	11.9	14.2	12.2	13.7	11.8	11.3
Operating CFPS (RM)	0.10	0.08	0.12	0.14	0.19	0.27	0.29	0.32	0.34
Free CFPS (RM)	0.10	0.08	0.12	0.12	0.03	0.02	0.01	0.07	0.09
P/CFPS (x)	12.2	19.1	10.8	9.1	7.4	6.2	6.1	5.5	5.2
DPS (RM)	0.03	0.04	0.04	0.07	0.07	0.07	0.07	0.07	0.07
Dividend yield (%)	2.5	2.4	2.8	5.6	5.2	4.3	4.0	4.0	4.0
BV/Share (RM)	0.82	0.87	0.87	0.98	0.96	0.99	1.11	1.21	1.32
Price/BV (x)	1.84	1.28	1.54	1.44	1.56	1.82	1.58	1.45	1.33
Weighted average shares (m)	4,577	4,577	4,469	4,526	4,522	4,450	4,513	4,513	4,513
Average market cap (RM m)	5,392	6,963	5,825	5,802	6,320	7,470	8,257	8,257	8,257
Enterprise Value (RM m)	4,233	5,689	4,325	11,257	12,649	14,826	16,999	16,910	16,756
EV/Sales	3.7	5.0	3.5	8.0	4.2	4.6	5.1	4.6	4.4
EV/EBITDA	5.7	8.3	5.9	13.6	7.8	8.0	8.8	7.9	7.6
EV/EBIT	6.9	10.1	7.1	16.7	11.4	11.2	12.7	11.3	10.6
EV/Operating Capital	1.6	2.0	1.5	1.0	0.9	1.0	1.0	1.0	0.9
INCOME STATEMENT (RM m)									
Sales revenue	1,137	1,147	1,228	1,414	3,000	3,204	3,364	3,695	3,830
Operating EBITDA	738	687	737	825	1,613	1,863	1,942	2,148	2,215
Depreciation	126	126	126	150	447	500	565	612	631
Amortisation	0	0	0	0	61	36	36	36	10
Operating EBIT	612	562	611	676	1,105	1,328	1,341	1,500	1,573
Net interest income (expense)	26	-28	-13	-53	-512	-488	-547	-585	-594
Associates/affiliates	0	0	0	0	1	1	141	211	211
Investment and other income/expense	1	1	1	1	65	3	3	3	3
Exceptionals/extraordinaries	2	2	8	23	-30	0	0	0	0
Income tax expense	44	154	169	161	183	230	256	327	346
Minorities/preference dividends	0	0	0	0	0	0	0	0	0
Net income	597	383	439	486	446	613	682	801	847
CASH FLOW (RM m)									
Cash flow from operations	442	365	540	637	859	1,211	1,311	1,445	1,537
Movement in net working capital	-325	-138	-49	32	-176	-45	-35	-73	-30
Capex	-1	-5	-3	-107	-738	-1,130	-1,283	-1,115	-1,145
Free cash flow	441	360	537	530	121	81	28	330	392
Other investing activities	0	17	-102	-13	-99	0	-543	0	0
Equity raised/(bought back)	0	0	-149	-45	-6	0	0	0	0
Dividends paid	-34	-229	-162	-161	-326	-326	-320	-325	-325
Net inc/(dec) in borrowings	-125	625	-125	7,824	1,502	1,262	1,444	276	251
Other financing cash flows	-23	-25	-12	-7,313	-666	-964	-1,202	0	1
Total cash flows from financing	-183	371	-448	305	504	-28	-79	-49	-73
Net cash flow	259	747	-13	853	529	53	-594	281	318
Movement in net debt/(cash)	-384	-122	-112	6,970	973	1,209	2,038	-5	-68
BALANCE SHEET (RM m)									
Cash and other liquid assets	2,305	3,052	3,038	3,891	4,421	4,474	3,880	4,161	4,480
Tangible fixed assets	2,920	2,799	2,676	11,205	12,511	13,976	15,980	16,483	16,996
Goodwill	0	0	0	0	441	441	441	441	441
Other intangible assets	0	0	0	0	0	0	0	0	0
Associates/investments	42	36	149	165	264	446	1,097	1,181	1,266
Other assets	399	433	503	943	1,037	1,243	1,270	1,394	1,444
Total assets	5,666	6,320	6,367	16,204	18,673	20,578	22,667	23,659	24,627
Interest bearing debt	1,188	1,813	1,688	9,511	11,013	12,275	13,719	13,995	14,245
Other liabilities	712	522	698	2,204	3,271	3,723	3,736	3,973	4,168
Total liabilities	1,900	2,335	2,385	11,715	14,285	15,998	17,455	17,968	18,413
Shareholders' equity	3,766	3,985	3,982	4,488	4,388	4,581	5,212	5,688	6,210
Minorities	0	0	0	0	0	0	0	0	0
Total shareholders' equity	3,767	3,985	3,982	4,488	4,388	4,581	5,212	5,688	6,210
Net working capital	-196	57	292	240	371	361	494	535	553
Net debt/(cash)	-1,117	-1,239	-1,351	5,620	6,593	7,802	9,839	9,834	9,765
Capital	2,650	2,745	2,631	10,108	10,981	12,382	15,051	15,522	15,975
RATIO ANALYSIS									
Sales growth (%)	5.2	0.9	7.0	15.2	112.2	6.8	5.0	9.8	3.7
Op. EBITDA/sales (%)	64.9	59.9	60.0	58.4	53.8	58.1	57.7	58.1	57.8
Op. EBIT/sales (%)	53.9	48.9	49.8	47.8	36.8	41.4	39.9	40.6	41.1
Payout ratio (%)	23.0	43.0	36.6	67.1	72.9	51.8	46.5	39.6	37.4
ROE (%)	16.7	9.9	11.0	11.5	10.1	13.7	13.9	14.7	14.2
Return on Capital (%)	21.5	15.0	16.7	8.2	7.7	8.3	7.9	8.0	8.1
Operating Return on Capital (%)	20.9	14.3	15.1	7.0	6.4	6.9	6.2	6.2	6.3
Capex/sales (%)	0.0	0.4	0.2	7.6	24.6	35.3	38.1	30.2	29.9
Capex/depreciation (x)	0.0	0.0	0.0	0.7	1.6	2.3	2.3	1.8	1.8
Net debt/equity (%)	-29.7	-31.1	-33.9	125.2	150.2	170.3	188.8	172.9	157.2
Net interest cover (x)	nm	20.0	47.8	12.7	2.2	2.7	2.5	2.6	2.6

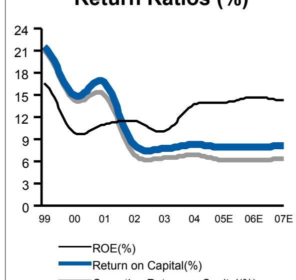
Price and Price Relative



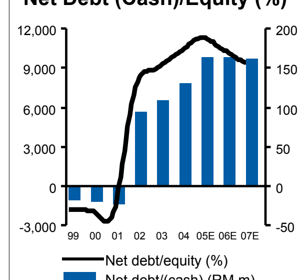
Margin Trends (%)



Return Ratios (%)



Net Debt (Cash)/Equity (%)



Source: Deutsche Bank AG estimates, company data

Investment thesis

Ingredients for a re-rating

We recently hosted meetings between YTL Power (YTLP) and investors in the US and UK. In our view, YTLP is emerging as one of South-East Asia's more interesting utility stories. Armed with RM4bn+ of gross cash, expanding expertise, a growing opportunity pool and a credible strategy, it has the necessary ingredients for a long-term re-rating. We upgrade our 12-month call to a Buy (more than 10% total return).

Newsflow has been getting positive. The pending acquisition of 35% in Jawa Power looks cheap and joins a favourable draft review of rates for Wessex Water. Next up, we believe another supplementary power purchase agreement (PPA) from Tenaga is a possibility. Further out, the group is emerging as a potential contender in Malaysia's water sector restructuring. We believe YTLP is also looking to build on its Indonesian exposure.

The stock has underperformed the UK water sector in 2004, despite the equally favourable draft tariff review. Market opinion appears indifferent on average; an 80/20 split between Holds and Sells on Bloomberg's 12-month recommendation list. Meanwhile, foreign shareholding is a low 2.5% (December 2003). This is a favourable set-up for investors willing to wait out the 'EB' overhang.

Valuation

With a net yield of 4% and low-risk earnings, YTLP is a defensive, long-term growth story at an undemanding FD PER of 11.8x in FY06F (10x basic). In addition to our 5-26% EPS upgrade, we raise the DCF/RAB-based target from RM1.85 to RM2.24 on the back of the UK Team's upgrade of fair water asset valuation from a 10% premium to RAB to 18%. We have also added Jawa Power (at effective 5.7x 2003 earnings.)

Our valuation does not include any 'option' value for the acquisition potential inherent in YTLP's RM4bn gross cash pile. This is probably too conservative from a long- to medium-term point of view. The group is clearly in acquisition mode and its opportunity pool is expanding. A potential supplementary PPA could mean a small upgrade in target, too.

Risks

A key stock overhang is the Exchangeable Bond, which is gradually being converted. This could cap near-term performance. Holders appear keen to pre-empt YTLP exercising its early redemption option, trying to keep the price under the trigger of RM1.77. Mitigating this, YTLP is buying back shares aggressively. This is value enhancing and could culminate in a stock dividend further out.

Other risks include rising bond yields (eating into the DCF), ringgit appreciation (lower translation of FX receipts), extreme rupiah volatility (raising paymaster risk at PLN) and re-negotiation of PPA terms. We view the latter as low. Whilst Tenaga is looking at ways to extract more value out of the PPAs, changing contract terms has system-wide consequences that could affect confidence in the market.

Valuation & recommendation

Upgraded to Buy; target price raised 21%

YTLP's target raised on the back of a higher assumed valuation for Wessex Water

We have upgraded our rating from Hold to Buy with 28% upside potential from the current share price on a 12-month horizon. We have raised our DCF/RAB-driven target price from RM1.85 to RM2.24 mainly on the back of:

(1) A higher Wessex Water valuation following the recent draft determination of water rates and use of RAB instead of DCF methodology, in line with our UK Water Sector research team.

(2) Inclusion of the Jawa Power acquisition in our model (at Indonesian cost of equity of 16.7% adjusted for 0.8x beta vs. an estimated IRR of 25%, giving PER of 5.7x 2003).

The biggest impact is from Wessex Water. Instead of using a DCF, we have decided to follow our UK Team's method of valuing the sector's regulated water businesses based on their regulated asset base (RAB). Following the favourable draft water rates review, our UK Team recently raised their sector fair value from a 10% premium to RAB to 18%.

The UK water sector has rallied in 2004 and companies covered by DB are currently trading above valuations derived simply using their most recent RAB (March 2004). See Figures 2 & 3 (where we have stripped out any premium to RAB). Adding further support, it was recently announced that National Grid Transco is in the process of selling four gas distribution networks at an average 15%+ premium to RAB.

Elsewhere, we are assuming Malaysia's cost of equity at 9.2% with YTLP beta of 0.57x. We are assuming terminal value for YTLP's IPPs with 20 years of cash flow at 40% of the last year of the PPA (2015). This reflects our view that the power plant will remain functional (given good maintenance record), but conservatively we assume returns will be substantially reduced as the industry is likely to be restructured by then.

Figure 1: Our valuation of YTL Power (1 year forward)

							RMm	Share total assets
Malaysia power generation	**Stake**	**Disc rate**	**FX**	**Rate**	**Basis**			
Paka, Terengganu & Pasir Gudang, Johor	100%	7.4%	-	-	DCF		4,912	23%
Indonesia power generation								
Jawa Power	35%	13.36%	US$	3.80	DCF		871	4%
Jawa Power O&M	100%	-	US$	3.80	Cost		14	0%
Overseas regulated utilities		**RAB Mar 05**				**Premium**		
Wessex Water, UK	100%	1652000000	GBP	7.60	RAB	18%	14,818	70%
ElectraNet, Australia, at est book value	33.5%	-	AUD	3.12	Book FY6/04		279	1%
Other assets								
Associates	-	-	-	-	Book FY6/04		0	0%
Other investments (est)	-	-	-	-	Book FY6/04		269	1%
TOTAL ASSETS							***21,162***	
Gross debt - FY05F							-13,719	
Gross cash - end FY05F							3,880	
Net debt							**-9,839**	
Total NAV - basic							**11,323**	
Shares o/s excl treasury shares		4,513						
FD shares		6056.31						
NAV adjustment upon conversion							2,254	**Per share RM**
Total NAV - FD							**13,577**	**2.24**

Note: Jawa Power will be an associate, hence the valuation above represents purely equity
Source: Deutsche Bank AG estimates, Company data

Figure 2: UK water sector – company valuations (priced 13 Sep 2004)

Bloomberg code (all LN)	**AWG**	**NWG**	**SVT**	**PNN**	**UU**	**KEL**	
	AWG	**Northumbrian**	**Severn Trent**	**Pennon**	**Utd Utilities**	**Kelda**	**Comment**
Water RAB	4,144	2,262	4,570	1,688	5,463	3,034	As of March 2004
Other business	188	181	815	166	1,977	264	DB UK estimate
Net cash	-3,191	-1,870	-2,749	-1,074	-2,929	-1,706	DB UK estimate
Total	**1,141**	**573**	**2,636**	**780**	**4,511**	**1,592**	
Value/share, GBp	**800**	**110**	**769**	**636**	**519**	**413**	**Assuming no premium to RAB**
Share price, GBp	660	145	847.5	813	555	514	As per Bloomberg
Premium	-17%	31%	10%	28%	7%	25%	
Av premium ex-AWG		20%					AWG is a restructuring story
Rating	Hold	Buy	Buy	Buy	Buy	Buy	
DB UK valuation, GBp (using RABtastic)	1,399	191	1,015	890	653	558	Assuming 18% premium to RAB and other efficiency adjustments

Note: This valuation is based on a report dated 5 August 2004, "UK Water: A Present for Everyone." We have taken out the 'RAB value adjustment' and updated the share price for 13 September 2004. Our UK Team has assumed no outperformance vs. either the regulator's opex or capex assumptions (also as per that report). The DB UK valuation line is not the official target which varies from case to case
Source: Deutsche Bank AG estimates, Company data, Bloomberg

EPS upgraded on Wessex Water and Jawa Power

Jawa Power is biggest factor behind the EPS upgrade

We have upgraded EPS estimates by 5% and 26% for FY05 and FY06 respectively. Wessex Water's higher rates for FY3-06F and five years forward boosts earnings. The inclusion of the 35% Jawa Power stake into our earnings model also gives it a lift, with eight months assumed for FY05F (effective 1 November). YTLP is buying this stake at a very undemanding PER of 3.5x 2003 earnings, sacrificing a mere RM12m in interest on cash for a net annual net profit contribution of around 150m. The NAV impact is not large because of the high cost of capital in Indonesia.

Cross-checking the target price

At the target price, the stock would be trading on a 12.6x basic PER in FY06F (Y/E June) for EPS growth of 17% that year (15.1x fully diluted). This compares with 12.7x basic PER for the Malaysian market in 2005F, with EPS growth of 16.7%. Given the group's longer-term growth potential, it deserves a premium to the market, in our view.

The 12.6x basic PER is a 10% premium to Malakoff's (MAL MK, RM6.20, TP RM7.10, Buy) 11.5x PER using the target price. We accord this premium to YTLP's broader long-term opportunity pool and higher financial flexibility, given its much larger cash holdings. Plus, it is worth noting that YTLP's PER multiples are distorted upwards due to the recognition of deferred taxation/employee benefits at Wessex Water which is mandated in Malaysia but not in the UK (MASB 25/29).

Applying a COE/ROE model, we reach a valuation of RM2.11 if we use the FY05F ROE of 14% and apply a beta of 1x to the market's COE of 9.2%. YTLP's actual 2-year beta is 0.57x, which highlights that this is a conservative estimate. Plus, the ROE has upside bias. We expect it to rise to 14.7% in FY06F given the full-year effect from Jawa Power and tariff hike at Wessex Water.

There is still potential upside bias to our target

No value accorded potential supplementary PPA

The more active YTLP gets on new investments, the higher the 'option value' on its substantial spare funding capacity

Our target NAV does not include any additional power sales to Tenaga. We believe Tenaga is exploring the prospect of taking more power from YTLP (in line with the Supplementary PPA, which expired 31 December 2003). A duplication of the Supplementary PPA would add around 3-4% to EPS in FY06F, assuming a full-year effect. The NAV impact would be +1-2%.

No option value imputed for cash

More importantly, we have not imputed any option value for YTLP's RM4bn gross cash pile relating to future acquisitions. With a longer-term view, this is too conservative. Not least because the company is signaling loud and clear that it is looking to gradually re-deploy part of its RM4bn gross cash pile. That means the drag on ROEs will ease. In our view, it will either use spare cash or use the cash pile to enable cheap financing. Conceptually, this cash pile will come in handy when interest rates rise, enabling fast deals. Plus, every 1% higher return on the cash generates about RM40m in additional interest income and raises the ROE.

YTLP's investment track record has been good and its know-how has expanded significantly since the early move to acquire 33.5% in Electranet (2000). This enhances the credibility of future moves. Case in point:

- Wessex Water has turned out to be a well-timed investment at a sterling rate in the region of US$1.40/GBp vs. the current US$1.80/GBp. YTLP bought it at a 9% discount to RAB in 4Q02, which compares with our in-house valuation of 18% premium today.
- The Jawa Power acquisition should also be value enhancing. The 35% stake is being bought at a 3.5x 2003 PER which is a fraction of the average 12.9x 2004F PER rating of the Jakarta Stock Exchange's seven biggest stocks, according to IBES consensus estimates on Bloomberg. These stocks account for 40% of the JCI index.

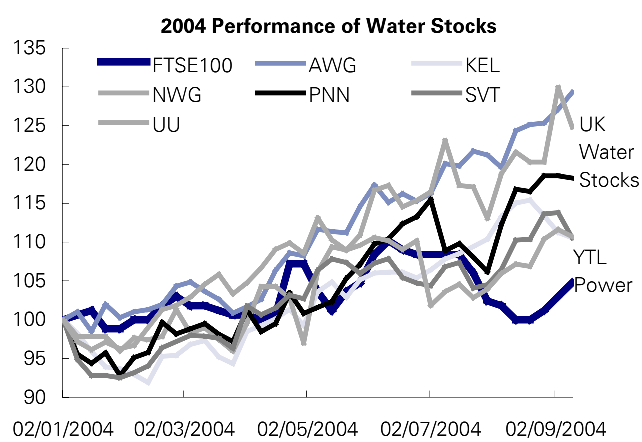
Regulated utility businesses remain in focus with a view to ring-fence risk away from the holding company. The strategy is to acquire assets that will strengthen the company's financial position and not affect its S&P rating.

However, the strategy has now opportunistically switched away from developed markets towards developing countries. This comes at a time when competition for regulated returns in developed markets has increased. The Jawa Power acquisition is an example. YTLP's intends to buy when markets are pessimistic and – more immediately – to exploit the vacuum in Asia created by players from the 'West' selling out. South-East Asia is preferred to North-East Asia, given there is less competition there.

Recently, YTLP was a front runner for National Grid Transco's sell-down of gas distribution assets, but dropped out prior to the final round as it deemed the pricing unattractive. In addition, there was uncertainty regarding the ultimate value of the individual areas' restructured RAB as National Grid had over-spent on capex in prior years. A CKI-led group recently clinched National Grid's North England zone for US$2.5bn, paying a 15% premium to the March 2004 RAB, whilst the other distribution areas were sold at 15.5-15.9% premiums.

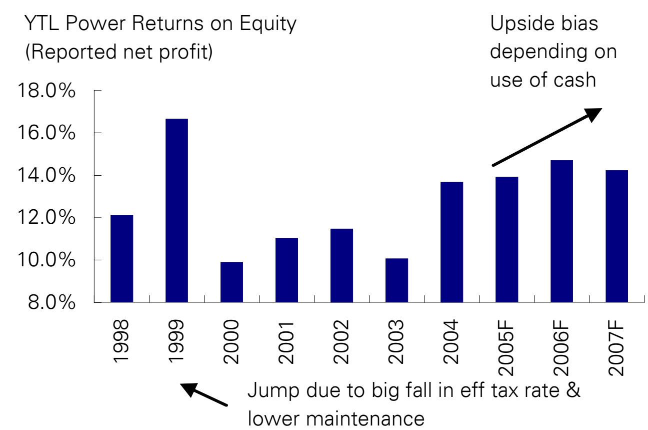
Looking at opportunities, the potential restructuring of the Malaysian water sector could provide an opening to YTLP on a 12-18-month horizon. Ahead of that, we expect YTLP could make further investments in the Indonesian electricity sector. YTLP is also scouting for opportunities in Australia and South-East Asia.

Figure 3: Strong run in UK water sector (indexed)



Note: share prices are indexed
Source: Bloomberg

Figure 4: YTLP's ROEs are heading up



Source: Deutsche Bank AG estimates, Company data

Technicals

It is worth noting that:

- YTLP has underperformed the UK water sector, despite having close to half of its NAV in Wessex Water.
- Foreign shareholding at YTLP is low at 2.5%. This compares with 26% for Malakoff ex-International Power's 19% stake. YTL Corp has an 18% foreign shareholding (all numbers are as of December 2003).

- There is not a single Buy recommendation on YTLP on Bloomberg's 12-month consensus: 80% are Holds and 20% are Sells.

Risks and overhangs

The share overhang

Share overhang partly neutralised by share buy-backs

There is one significant stock overhang: conversion of the US$150m exchangeable bond (EB) which matures on 11 July 2006. The EB has seen a wave of conversions, starting early in FY04 as the share price traded north of the RM1.475 exercise price. Out of the US$150m bond, 25% has been converted, leaving 290m in potential share conversion (vs. the full 386m). This is 6% of total shares outstanding. The warrant issue is much bigger at 1.1bn shares and is also in the money, but matures in 2010 and is unlikely to see much conversion in the near to medium term.

YTLP has an option to call the exchangeable bonds if the stock trades above RM1.77 for 20 consecutive days. We understand EB holders have been converting their EBs in an effort to keep the share price from appreciating. This has exacerbated the overhang. Management is now considering its strategy towards this issue.

At first glance, the remaining conversion appears daunting. It represents 161 days of average volume (as per the past six months). However, YTLP has been mopping up the liquidity via share buy-backs. In FY04 alone, it bought back 107.2m shares, representing 2.3% of shares outstanding at the start of FY04. Since the end of June, it has bought back another 15m. Combined, that represents 127% of the 96m shares converted from the EB since the start of FY04. The annual mandate is 10% of shares outstanding, leaving room to continue this exercise. To mop up the rest would cost RM508m. From a return perspective, buying back the stock is both NAV and EPS enhancing, given the return on cash of about 3% pretax vs. the 6% pretax yield on the stock.

Figure 5: Current status

Exchangeable bonds	FY03	FY04	FY YTD FY05
Outstanding, US$m	150	143	113
Conversion price, RM/share	1.48	1.48	1.48
Converted value, US$m	0	7	31
Converted shares, m	0	18	79
Remaining value, US$m	150	143	113
Remaining shares, m	386	369	290
As % of total outstanding			6%
Treasury shares, m	56	163	178
Shares bought back, m		107	15

Source: Company data, Bursa Malaysia

We understand that the shares bought back could be offered to shareholders as a dividend at some point, restoring the free float.

A collection of risks, too

There are several risks to the share price and our target valuation, including ringgit appreciation, extreme rupiah volatility, rising bond yields and re-negotiation of the PPA between its IPP and Tenaga.

Ringgit appreciation would hit the translated value of earnings from both Wessex Water and Jawa Power. But this is unlikely in the near term and even if it happens, the impact is mitigated by our view that the ringgit is only undervalued by 3-5% at the most (on a real effective basis). On a related point, Jawa Power's fundamentals would be negatively affected should the Indonesian rupiah go into free fall, given the impact on Perusahaan Listrik Negara's (PLN) ability to pay.

Rising bond yields would eventually mean analysts having to raise their discount rates, which would primarily hit the Malaysian IPP valuation – every 1% higher risk-free rate would erode NAV by around 1% (assuming the Wessex Water valuation remains constant).

PPA re-negotiation risk has re-surfaced but we remain of the view that it is small. The government is unlikely to change the PPAs as this would negatively affect investor sentiment at a time when it is looking to raise a lot of money to fund the water sector restructuring. There are more stakeholders involved, which complicates matters – e.g. the holders of the non-recourse bonds (primarily EPF). The bottom line – this would be a small benefit to Tenaga but a potential loss of market confidence.

Wessex Water

A positive draft tariff review

Draft tariff review sets tone for final determination in December

The UK Water Regulator (Ofwat) issued its draft determination of water rates on 5 August 2004. This outlines the regulated water rates and capex programmes effective April 2005 and five years forward. Indications that water tariffs are to be raised caused the sector to extend its 2004 rally. We recall that the market had been expecting the regulator to take a more 'equity-friendly' stance after a period of ownership instability (e.g. which led to Enron's sale of Wessex Water to YTLP). The final determination will be announced in December and is only likely to present minor adjustments of the draft review.

Figure 6: Wessex Water's tariff increases; past and future

Year to March

The 2000-05 Period	2001	2002	2003	2004	2005	Average
Price limit (k), %	-12	0	0	3.8	4.7	-0.7
Capex / property / year, £	183					

The 2006-10 Period*	2006F	2007F	2008F	2009F	2010F	Average
Price limit (k), %	7.4	3.9	4.6	3.3	2	4.2
Capex / property / year, £	184					
Capex total, £m	727					

**As per interim tariff determination announced 5 August 2004*
Not official yet - it will be firmed up by December
Price limits are before inflation. In addition to the k factor, utilities will adjust up prices by RPI increase in the preceding November period
Source: Ofwat

According to Ofwat's draft determination, Wessex Water will get an average annual price increase of 4.2% vs. its request of 6.5%. This is seen as a good result. The average annual price increase of 3.1%+ RPI compares with the average request of 6.2%+ RPI for the sector. During the previous 2000-05 tariff period, Wessex Water had -1% Cagr in water tariffs.

The capex programme suggested in the interim review totals £727m over five years. This compares with £915m in the previous period and Wessex Water's request of £900m+ for 2005-10.

Iain Turner of DB's UK Team said: "We deem the draft price proposals good news for the sector, [they] remove uncertainty and show that the regulatory process is working in a transparent manner, which treats the aspirations of capital providers fairly. This is in stark contrast to the approach five years ago."

Mr Turner indicates that Ofwat's headline average cost of capital for the sector is 5.1% (real post-tax) and 5.5% with allowance for 'financeability'. This compares with DB's base case of 5.0% (real post-tax). This is up from the 4.75% real return the regulator allowed in the 2000-05 period.

Ofwat outlined sector capex of £15.7bn vs. company requests of £21bn (as a number of schemes have been taken out of the programme). Mr Turner indicates that if the lower capex programme is caused by requiring fewer schemes then the overall price increases appear slightly better than expected, helped by the slightly improved cost of capital assumption. The UK Government may ask for the capex programme to be increased but DB expects higher price increases as a result.

The main downside, Mr Turner indicates, is that several operators expressed concern that they might struggle to outperform the regulator's targets on opex. But this is still subject to negotiation.

Our UK Team raises its valuations
Our UK Team subsequently raised its fair value assumptions for the sector. It now assumes an 18% premium to the RAB at the enterprise value level (equivalent to a 40% premium at the equity level, assuming 55% gearing). This is up from 10% previously.

What is a RAB?

This is taken from Richard Smith's report "Global RABtastic 2004: Europe still offers best value" dated 16 January 2004.

> "Regulation of network utilities has generally been guided by the desire to provide sufficient revenue to fund the capital and operating expenditures required to deliver quality utility services to customers without permitting the company to earn excessive 'monopoly' profits for an extended period of time. Part of the revenue under all regulatory regimes is supposed to remunerate the capital invested in the business. The question is, how much capital is invested in the business? Different countries calculate the regulated asset base in different ways. We discuss the methodologies in more detail below.
>
> UK utilities were privatised in the period 1989-1993 and their new owners (shareholders) did not, by and large, pay book value to acquire them. To get around this (and not hand massive profits to the new owners), regulators have adjusted book value, recognising what was paid to acquire the companies, to create the RAB. Most regulators have recognised that the government deliberately underpriced the flotations to ensure their success and have, therefore, incorporated an uplift into the initial RABs. The company is then allowed to earn a return on this RAB, rolled forward to reflect new capex and depreciation.
>
> The depreciation charge is also a specific regulatory construction, rather than a figure shown in the accounts, again due to the difference between book value and RAB. There have been differences between the regulator's (and MMC's) approaches to calculating initial RABs, as well as methodological differences on depreciation. In the past, RABs have been subject to some uncertainty, but these are now all settled. The RAB value for each company included in our analysis is taken directly from regulatory documents produced either by Ofgem (for electricity and gas utilities) or Ofwat (for water utilities)."

Malaysia water opportunity

YTLP emerges as potential water play

Water remains a 'conceptual' opportunity but could happen sooner than generally expected

The long-term logic of the Wessex Water acquisition is now abundantly clear. Malaysia is in the early stages of revamping its water and sewerage services sector. This is an urgent exercise, given the weak state of water services in many states after partial privatisation in the 1990s. There is talk of water shortages looming over the next three-to-five years in Selangor's Klang Valley if nothing is done. The existing structure is financially unsustainable in many areas. The lack of central planning and lack of incentives for efficiency are at the core of the problem.

Overview of current state of affairs

Government to tackle fragmented industry

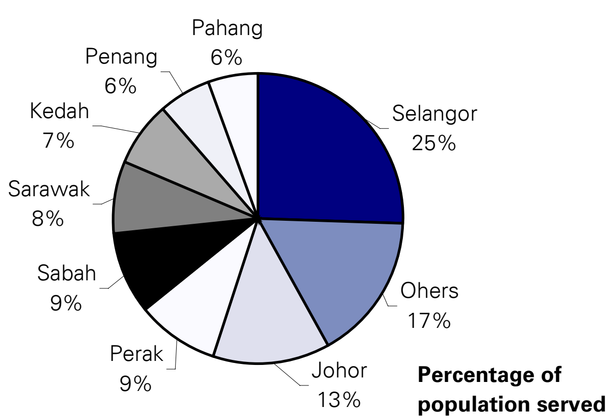
Current water set-up is not sustainable in the longer term for most states

The current set-up is very fragmented. Each state has full control over its own water resources and there is little inter-connectivity. There is no federally driven tariff or regulatory harmonisation. Water areas are divided up according to state boundaries. There is also an almost complete reliance on water from rivers, something that necessitates investment in processing facilities. This is more expensive than ground water as more chemicals and equipment are involved.

Effectively, there are three 'models' in place:

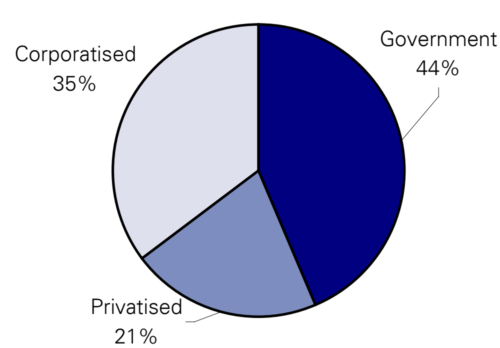
- Penang and Johor opted for privatisation of integrated services from sourcing to distribution.
- Selangor, Terengganu and Sarawak (Laku) have privatised bulk water supply, whilst maintaining distribution in state hands. The private suppliers collect water from rivers and clean it before handing it over to the states.
- Elsewhere, water sourcing and distribution remains under state control (via public works departments or water supply boards). Kelantan privatised its water operations in 1995 but the state government bought back Thames Water's 70% stake in 1999 after public complaints, mounting debts and high non-revenue water.

Figure 7: Relative size of states 2001



Source: Malaysian Water Association

Figure 8: Type of state water entity 2001



Note: 'Corporatised' is a mix of private and government

Source: Malaysian Water Association

Penang and Johor have differed from the rest

Integrated models have been more successful

The integrated Johor and Penang models are seen as relatively successful. Ranhill Utilities owns SAJH in Johor and is profitable. In Penang, the state government owns 55% of PBA Holdings Bhd, a profitable listed company that took over from the Penang Water Board. Penang has the lowest non-revenue water rate in Malaysia, currently at about 22% vs. a national average of about 40%.

Figure 9: Financial performance of the Malaysian water sector 2001

RMm, 2001	Revenue	Opex	Op'r profit	Margin
Labuan	9.7	16.1	-6.4	-66%
Perlis	10.5	12.3	-1.8	-17%
Sibu	18.6	18.4	0.2	1%
Sarawak	19.9	30.3	-10.4	-52%
Kelantan	41.5	30.5	11	27%
LAKU (Sarawak)	43.3	40.7	2.6	6%
Sabah	51.7	175.3	-123.6	-239%
Kuching	57.5	53.8	3.7	6%
Terennganu	74	38.8	35.2	48%
N Sembilan	77.3	61.2	16.1	21%
Melaka	94.3	68.6	25.7	27%
Pahang	96.1	102.8	-6.7	-7%
Kedah	133.1	97.7	35.4	27%
Penang	163.3	104.1	59.2	36%
Perak	186.1	167.6	18.5	10%
Johor	416.4	251.4	165	40%
Selangor	733.9	1495.2	-761.3	-104%
Total	**2227.2**	**2764.8**	**-537.6**	**-24%**

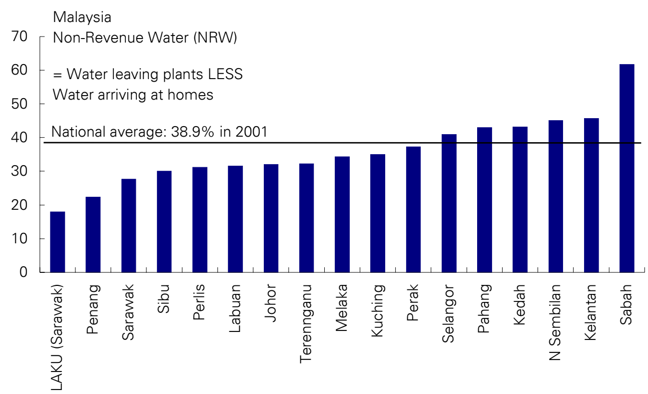
Note: Data may seem old, but this is the latest available. Generally, the state of affairs has not changed, from what we can tell from press sources. Financial conditions are likely to have deteriorated
Source: Malaysian Water Association

Non-integrated models prone to problems

In states where there is a split between bulk water suppliers and distribution, financials are weaker. This is particularly the case with Selangor. In 2001, as seen in Figure 9, Selangor lost RM761m at the operating level vs. profits of RM165m and RM59m for Johor and Penang, respectively. This is before financial costs. The situation is critical because Selangor services 25% of the population, including Kuala Lumpur, and is by far the most economically important state.

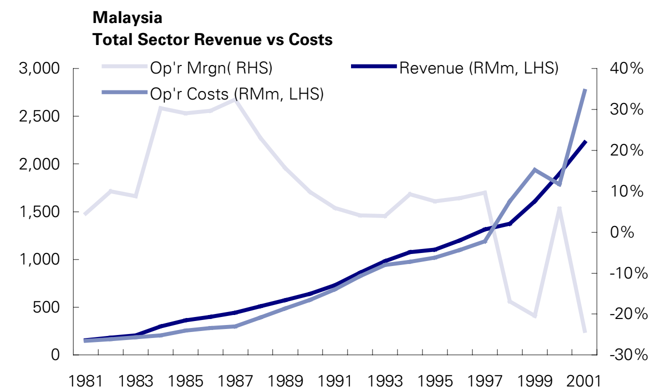
It is interesting to note that Selangor's losses are despite having the third- and second-highest domestic and industrial tariffs, respectively, in Malaysia. Johor has a higher tariff, but Penang is at the bottom of the league in both categories (according to our data, as per Figure 13).

Figure 10: Non-revenue water in Malaysia 2001



Source: Malaysian Water Association

Figure 11: Losses are mounting



Source: Malaysian Water Association

Key problems: NRW and flawed incentive structure

Incentives must be aligned from sourcing down to billing

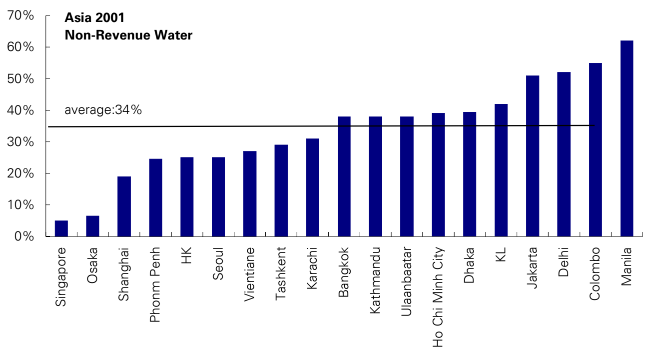
In addition to sticky water rates, poor financial performance is due to high non-revenue water (NRW). NRW is water revenue lost due to leakage, theft and inaccurate billing. Malaysia had 39% NRW as of 2001 vs. an Asian average of 34% (as per Figure 12). We understand this ratio has not changed much since then.

A higher NRW means more investment in expensive 'upstream' processing capacity and higher costs due to inefficiency. A key problem is old pipes and other infrastructure. NRW cannot be eliminated totally, but a reduction towards the ideal range of 15-20% could mean large financial benefits. A loose analogy can be made in the case of Penang. It has only average billing per customer (Figure 13), but has high margins. This is due to it having the second-lowest NRW. Johor has higher margins, but largely because its billing/account is 31% higher than average. Johor's NRW was 32% in 2001 vs. 22% for Penang.

In a non-integrated model, the incentives are skewed. The private companies that supply the bulk water have had an incentive to push as much water down the network as possible. They are not directly affected by NRW. The state governments are left to deal with that. These in turn are unable to fund necessary capex to lower NRW because water tariffs are hard to raise. This is a vicious cycle as less capex means lower water quality and service levels over time. Consumers are then even less willing to pay more. In addition the NRW problem means poor financials, mounting receivables and the need to pump even more water through the network, i.e. building even more processing plants.

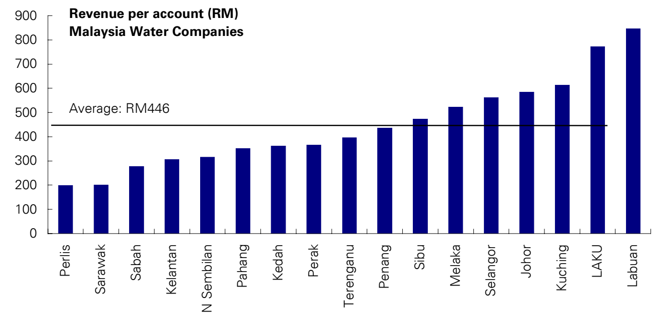
The problem is compounded by weak collection infrastructure and lack of efficiency targets. Case in point, the Selangor State Government owes its water suppliers RM2bn, of which Puncak Niaga accounts for RM1.3bn.

Figure 12: An Asian NRW comparison



Source: Malaysian Water Association

Figure 13: Water bill comparison – Malaysia



Source: Malaysian Water Association

The way forward

Government freezes further changes – UK model proposed

Government now reviewing how to manage the sector going forward

With mounting concerns about the state of the sector, the Ministry of Energy, Water and Communications suspended awards of any water privatisation deals earlier this year, pending a full review. This put a halt to individual state government's efforts to privatise their water services. For example, Puncak Niaga was due to take over Selangor state's distribution company, PUAS (Syabas). Furthermore, the minister in charge, Datuk Seri Lim Keng Yaik, proposed that Malaysia should use the UK framework of water privatisation as a model after a fact-finding trip to the UK and France.

The UK privatised its water and sewerage sector in 1989. At that time, the industry was not that much different from the situation Malaysia faces today, e.g. high water losses and consumer complaints. The UK model is fully integrated with companies responsible for sourcing of water right down to billing customers. Tariffs are set by a transparent regulatory regime for the entire country based on cost of capital assessments and capex, which enables predictability and a low cost of capital. In addition, water concession borders are based on natural supply and demand demarcation, not along municipal/provincial lines. Companies are heavily leveraged, but because of low operating risk, systemic risk is greatly reduced.

The ball is already rolling

The ultimate shape of the privatisation remains unclear. Clearly, the government must make allowances for local conditions. Nevertheless, the ball is already rolling. The government is now looking to change the constitution enabling the transfer of water rights from the state governments to the federal government. This could happen by the end of this year. Meanwhile, the long-awaited Commission of Water Services Malaysia will be established by early 2005, according to statements in the press. The Water Commission will have responsibility for central planning, regulations and water tariffs, in line with the UK's Ofwat. After that, the blue print will be rolled out. All of this could happen by the end of 2005. We believe the guiding idea is to have an open tender for concessions, very much in line with PM Datuk Seri Abdullah Badawi's 'transparency' drive.

Capital markets to fund build-out

Transparency is key if build-out is to be financed via bond market

The official, preliminary plan is to spend RM50bn over the next ten years to overhaul water services nationwide. This includes a hefty amount for pipes to solve the NRW problem. If the UK model is followed, the bond market will fund the build-out, leveraging off of high regulatory transparency to bring down cost of debt, potentially via 'perpetual' instruments. This would enable instant tapping of Malaysia's vast pent-up liquidity and is similar to what Malaysia did with the IPPs in the early 1990s. This could herald another quantum leap for the domestic capital markets.

Some serious hurdles to overcome

Aside from concerns over rising water rates, a key hurdle is what to do about pending privatisation at the state level, e.g. PUAS and, more pressing, existing concession holders. There is also the issue of merging sewerage services into the whole (currently it is under Indah Water). The government has talked about reviewing existing contracts, raising the possibility that terms will be changed. Generally, visibility here is low.

We speculate that the government could retain the Penang and Johor situation, but amend the concession areas and bring these into the fold of national regulations, harmonising tariff, capex and efficiency targets. The states that have not been privatised would see concessions open up for bid under the federal umbrella, whilst Selangor could see a more radical solution, given the pressing state of affairs. In Selangor, the federal government has more leverage, given that the state cannot pay back the RM2bn it owes the water processors. The government has now indicated that it will take over this liability.

Whilst there is the prospect of a rise in water rates given that massive infrastructure spending, longer-term tariff pressure could be mitigated or even offset by efficiency savings. If NRW gets cut by half in Selangor (from the current 45%), that state could end up saving around RM200m annually, in our estimation. That in turn could support a RM2-3bn financing package.

How does YTLP fit in?

YTLP would be a strong contender if open bidding is allowed for concessions

YTLP is the only Malaysian company with direct experience of the UK model. Hence it could immediately mobilise the necessary know-how. Plus it is worth noting that Wessex Water is currently the most efficient water and sewerage utility in the UK. It is safe to assume that YTLP will be bidding, if new concessions are indeed offered – and we would count them as a strong contender.

YTLP likely to emerge as a water concept play in the next 6-12 months

It is much too early to speculate on the financial impact. This is a long-term story and falls under the 'option value' category that comes from its spare funding capacity and water expertise. Nevertheless, given that the government is likely to firm this up on a fast-track basis, the market is likely to start imputing some positive value in the frame of our 12-month stock call horizon. In our view, YTLP is likely to emerge as a water concept stock before long.

Indonesia, the new frontier

Bargain hunting amid pessimism; Jawa Power is only the start

35% stake in one of Indonesia's most modern power plants

Indonesia represents a new frontier for YTLP. It is now finalising the purchase of 35% and 100% of Jawa Power (JP) and the Operations & Maintenance (O&M) company for US$139.4m and US$3.6m, respectively. Included in the JP deal consideration is US$17.1m of subordinated, unsecured loan stock yielding 15% annually. Also part of the acquisition, YTLP has entered into an agreement whereby it may be required to purchase US$60m of bonds issued by Jawa Power from certain lenders (under a put option).

The seller is Powergen. Jawa Power is Powergen's last asset in Asia and it is being sold for strategic reasons. The other shareholders are PT Bumipertiwi Tatapradipta (15%) and Siemens (50%).

What is Jawa Power?

Jawa Power owns a 1,220MW coal-fired plant at the Paiton complex, in the east-most end of Java. These are the newest generators in Indonesia. This complex comprises Jawa Power (Paiton 2) and International Power's Paiton 1 (acquired recently from Edison Mission).

The power plant is directly connected to the Java-Bali grid. All the coal is supplied from domestic sources. The electricity is sold to PLN under a 30-year PPA initially signed in 1995 (and amended in 2002) with a 'letter of support' from the Indonesian Government. The payment track record since commercial operation in November 2000 has been clean.

The PPA expires in November 2030. This is structured along the lines of capacity and energy payments with full fuel pass-through to PLN. Profit and returns are largely captured in the capacity payment with a small margin in the energy payment depending on efficiency of coal burning. There is no direct FX risk as the PPA is structured using US dollars. The project also comes with political risk cover for debt holders.

Profitability and dividends

Jawa Power generated a profit of US$110m in 2003, up from US$105m as utilisation rates increased from 64% to 70% (with actual availability of 90% vs. 89% in 2002) and net interest decreased. YTLP's 35% stake would thus have yielded a net profit of RM146m in 2004. The US$17m loan stock gives another RM10m in pretax profit. Meanwhile, the dividend rate is healthy. For FY03 (Y/E December), Jawa Power paid an interim dividend of US$71m, representing a pay-out ratio of 65% of net profit.

The O&M company generated a net profit of US$2.2m in 2004 on turnover of US$9.6m.

Valuations cheap, but risks appear well padded

Cheap acquisition …

The acquisition appears cheap on a PER basis and is both NAV and EPS enhancing. We estimate a PER of 3.4x 2003 earnings for the two companies, including the loan stock. We estimate the investment IRR at 25%, significantly outperforming the 16.7% country cost of equity.

We assume the 2003 rate of earnings in our forecast, which should give YTLP net profit of RM161m, before deducting interest lost of RM12m. However, given power shortages, utilisation rates may rise, lending a little bit of upside bias to YTLP's bottom line. The acquisition will contribute about 22% to full-year bottom lines with an 8-month effect expected FY05F.

Clearly, Indonesia is not without risk

... reflects risk, but price appears to be discounting too much

Clearly, Indonesia is not without risk, which is why the acquisition comes cheap. But it looks more like a function of aversion to Indonesia's country risk, few natural buyers and a seller keen to get out of Asia as a whole. YTLP is clearly taking a view that the bottom has been reached.

We think country risk is significantly mitigated by what appears to be a relatively low-risk PPA and Jawa Power's priority status on the merit order of dispatch (due to age of plant). Risk is also reduced now that the IPPs have re-negotiated their tariffs and after PLN's own tariffs have started to rise. More significant, however, is probably Indonesia's growing electricity shortages.

Figure 14: Demand and supply – the Java-Bali grid

Java-Bali	2001	2002	2003	2004F	2005F	2006F
Energy sales (TWh)	69,120	74,820	81,740	89,270	97,470	106,220
Growth		8%	9%	9%	9%	9%
Peak demand (MW)	13,326	14,174	14,862	15,844	16,965	18,168
Growth		6%	5%	7%	7%	7%
Number of customers (m)	20.12	20.78	21.74	22.8	23.95	25.16
Growth		3%	5%	5%	5%	5%
Available capacity, MW			18,608.9			
Effective capacity, MW (our estimate)			15,608.9			
Reserve margin - available capacity			25%			
Reserve margin - effective capacity			5%			

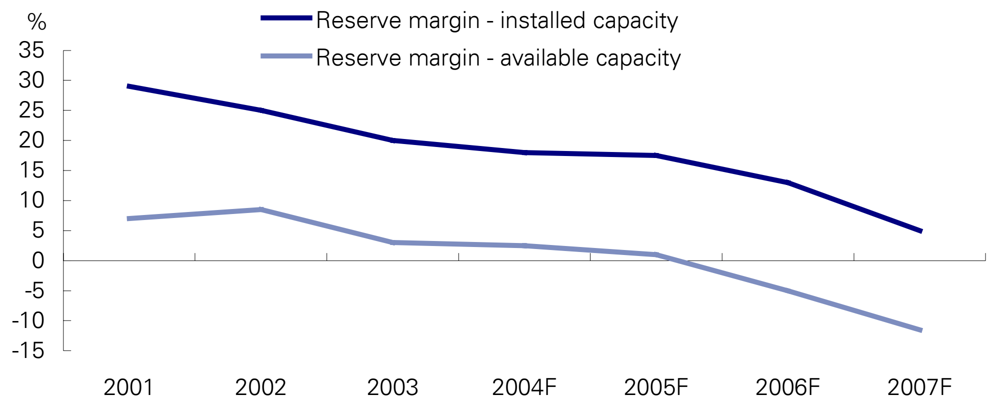
Source: Various press sources, PLN's forecasts

Electricity sector in critical state, which mitigates risks for IPPs

Indonesia facing power supply problems

The supply/demand imbalance in Indonesia is growing. The Bali-Java grid accounts for about 80% of demand and has had little net, new capacity added since at least 2000. The outlook until 2007 is largely flat, according to a presentation by Keppel Corp (in conjunction with its now-defunct proposal to buy the Jawa Power stake). This is perhaps not surprising, given years of under-investment, wrangling over power tariffs and currency weakness. Indications last year suggested that the 1,320MW Tanjung Jati B coal-fired plant would not come on stream until 2006, but even that was uncertain. Meanwhile, peak demand is growing at least 7% p.a. (based on PLN's low scenario forecast) and power outages are frequent in some areas.

Figure 15: Indonesia's reserve margin



Source: Taken from the Keppel Corp presentation for analysts when it announced the purchase of 35% in Jawa Power (prior to YTLP). They in turn cite ING as a source

A low and falling reserve margin

Reserve margin down to critical levels

As a consequence, Indonesia's reserve margin is tumbling fast. On top of this, much of the existing capacity is in need of overhaul. In a report last year by the US Embassy in Jakarta, PLN indicated last year that out of a total 18,609MW of capacity in Java-Bali, some 3,500MW is perennially out of commission due to maintenance.

Hence whilst the headline reserve margin is currently just less than 20% – that is already a low level for a fast-growing country – the effective reserve margin is probably less than 5%. The situation is compounded by reliance on hydro power during peak demand periods (accounting for 14% of capacity). Drought conditions, e.g. during El Nino episodes, significantly cuts power generation potential from these. Demand management and taking power from captive power generators alleviates the problem, but only in the short term.

Hence, the country urgently needs to attract more investment. That means there should not be much room for changes to existing PPA contract terms. Investor sentiment is fragile enough as it is. As a further consequence, expansion prospects in Indonesia appear good, with above-average IRRs expected.

35% stake in Jawa Power is only the start

YTLP is likely to use Jawa Power as a springboard for further expansion

PLN has expressed interest in using rupiah-based financing for power plants. This augurs well for YTLP as it was the first in Malaysia to use indigenous currency financing for IPPs. The Malaysian model helped the country ride through the 1997/98 crisis. Hence, leveraging off its Jawa Power stake, there is good chance for the group to secure robust longer-term returns. We also believe there is a good chance for YTLP to raise its stake in Jawa Power itself. The Indonesian shareholder and Siemens are unlikely to hold on to their stakes in the medium to long term, in our view.

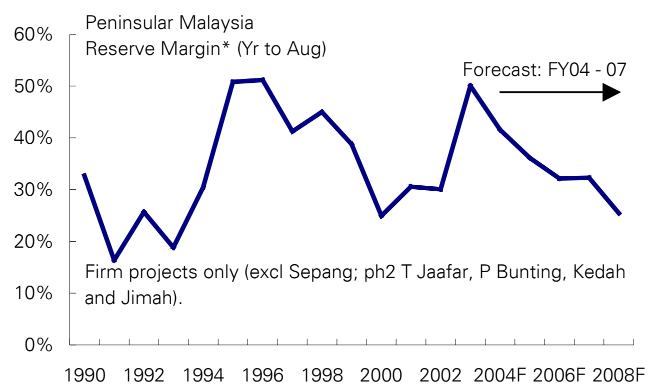
Malaysia IPPs

Tenaga may want to take more electricity

Malaysia does not offer much in the way of new power projects ...

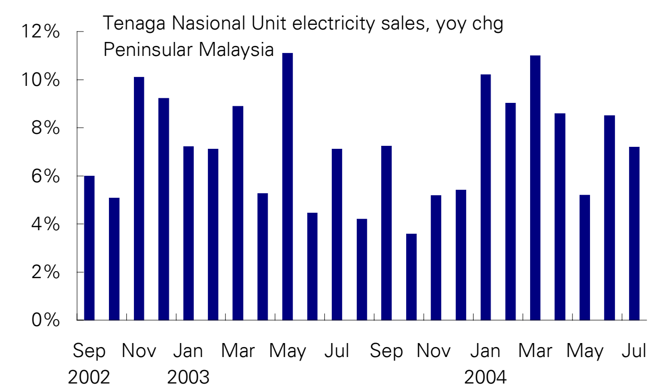
The Malaysian power sector does not really offer any interesting expansion opportunities for YTLP for the time being. A high reserve margin and projects pencilled into 2010 mean the prospect of new PPAs is small. Industry restructuring is a long-term game and way too early to speculate upon.

Figure 16: Reserve margin high but has peaked



*Excess supply/peak demand
Source: Deutsche Bank AG estimates, Tenaga Nasional

Figure 17: Demand momentum robust



Source: Tenaga Nasional

... but YTLP may have a chance to raise utilisation of its existing asset

We believe Tenaga is exploring the possibility of taking more power from YTLP's two existing power plants (total 1,212MW). Tenaga is in the throws of a revamp/cost-cutting exercise. In addition, with average coal costs rising from US$34/mt to an estimated US$45/mt in FY05F (Y/E August), it is keen to raise off-take of gas-fired power plants.

This is what was done in the supplementary PPA which expired on 31 December 2003 (1,200GWh over three years). This contract represented 14% of electricity supplied during FY02 and FY03 and was transacted at a price of 10.90 sen/kwh, significantly below the 15.5 sen YTLP gets on working days under the existing take-or-pay contract (70.2% of 1,212MW).

Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist			
Company	**Ticker**	**Recent price**	**Disclosure**
YTL Power Intl Bhd	YTLP.KL	RM1.75	8,9
Malakoff	MAL MK	RM6.20	9
Tenaga Nasional	TNB MK	RM10.900	7,8,9,13,14

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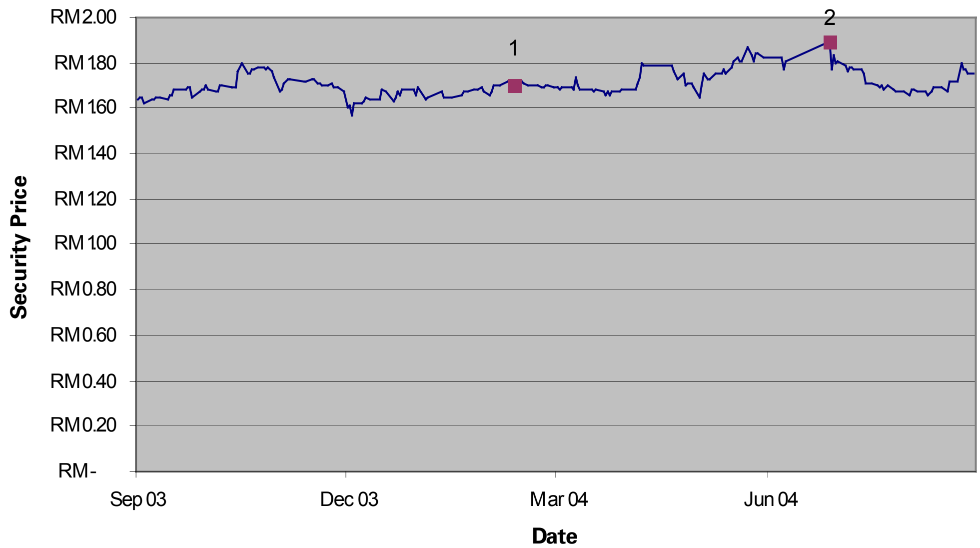
Historical recommendations and target price: YTL Power (YTLP.KL)

(as of 9/13/2004)



Previous Recommendations

Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9, 2002

1. 26/2/2004: Hold, Target Price Change RM3.70 2. 12/7/2004: Hold, Target Price Change RM1.85

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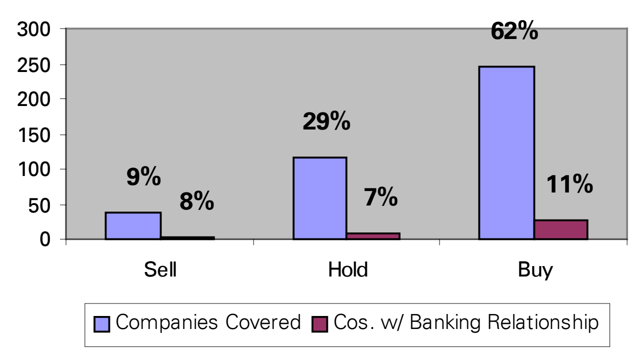
Buy: Total return expected to appreciate 10% or more over a 12-month period

Hold: Total return expected to be between 10% to –10% over a 12-month period

Sell: Total return expected to depreciate 10% or more over a 12-month period

The target prices of shares mentioned in the accompanying text are based on the assumed investment horizon of 12 months. If company notes are published on these shares in the future, the target prices mentioned in the subsequent notes will have priority.

Rating dispersion and banking relationships



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