



Filepic of Gas Malaysia office in Shah Alam, Selangor. The commencement of the IBR by Gas Malaysia is expected to be similar to that applied by TNB.

IBR's impact on Gas Malaysia is neutral short term

**Gas Malaysia Bhd
(Oct 23, RM2.44)**

Downgrade to hold with a target price (TP) of RM2.42: Gas Malaysia last Thursday announced the commencement of an incentive-based regulation (IBR) that will take effect on Jan 1, 2016.

The IBR is a form of economic regulation initiated by the government aimed at incentivising Gas Malaysia for better operational and financial performance, while regulating the natural gas tariff. It is introduced to promote efficient resources allocation and usage, and sustainable financial performance.

Next year will be the trial run period for the IBR and the first regulatory period will run for the next three years from 2017 until 2019.

However, overall mechanism is still pending the finalisation by the Energy Commission and we expect Gas Malaysia will provide further information on the IBR mechanism in the short future.

The commencement of the IBR by Gas Malaysia is expected to be similar to that applied by Tenaga Nasional Bhd (TNB).

To recap, on the IBR, TNB

takes into account the efficient cost (capital expenditures and operating expense) in the tariff calculation and introduces incentives or penalties on the operational performance.

This efficiency gains will be shared between consumers and the company. The IBR comprises a base tariff, which generally reflects the capital expenditure plus operating expense and imbalance cost pass-through (ICPT) for adjustment to reflect the change in uncontrollable cost from the base tariff.

We view the IBR on Gas Malaysia to be neutral short term, but positive long term, following the fact that it will ensure further security on the company's revenue stability and protect it against the fluctuation of natural gas price in the future.

Hence, we are maintaining our TP of RM2.42 based on a dividend discount model with weighted average cost of capital of 7.9%, which implies a 21.7 times price-earnings ratio of 2016 earnings per share with a "hold" recommendation following the recent price uptrend. — *BIMB Securities Research*