

## V.S. Industry (VSI MK)

# No surprises in 3QFY22 results

### Results in-line; Maintain HOLD

VSI 9MFY22 results came in within our expectations but missed the street's estimates, making up 73%/67% of ours/consensus' full-year forecasts respectively. We maintain our earnings assumptions and TP of MYR1.07, derived by pegging its fully-diluted FY23E EPS of 6.4 sen to a PER multiple of 16.7x, in-line with the company's 5-year historical PER mean. The company's near-term outlook is weighed down by on-going labour issues, raw material shortages and increasing cost pressures. However, we believe the light at the end of the tunnel is near, with the arrival of foreign labour in 4QFY22. We prefer ATECH (BUY, TP: MYR2.03) for our EMS pick.

### Labour and component shortages dragged sales

VSI's 9MFY22 core net profit (CNP) came in at MYR134m (-35% YoY). The earnings contraction was mainly down to lower order deliveries due to labour/component shortages and higher depreciation costs. Meanwhile, its 3QFY22 CNP of MYR53m (+24% QoQ, -28% YoY) came in higher QoQ despite lower revenue (-9% QoQ, -14% YoY), thanks to improving margins attributable to a more favourable product sales mix.

### Diseconomies of scale hurting profitability

Zooming in on its geographical performance, Malaysia segment's 9MFY22 revenue shrank by 3% YoY as order deliveries reduced, hampered by shortages in labour and components. Likewise, PBT slumped by a larger 37% YoY due to diseconomies of scale and higher input costs (ie. labour costs, raw material costs and depreciation costs have all increased). The Indonesia and China segments remained lacklustre, as a result of lower sales orders and diseconomies of scale respectively.

### Rising costs and inflation headwinds ahead

While we believe VSI's labour shortage concerns will start to ease with the arrival of foreign workers in the coming quarter, its recovery process from the operational disruptions could be bumpy as rising costs and inflationary pressures are likely to affect its near-term margins and dampen consumer demand for the premium consumer electronic products it assembles, respectively. Hence, we maintain our HOLD recommendation for VSI.

FYE Jul (MYR m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	3,243	4,002	4,356	4,940	5,364
EBITDA	227	439	355	471	552
Core net profit	105	274	182	277	342
Core FDEPS (sen)	2.8	7.3	4.3	6.4	7.8
Core FDEPS growth(%)	(74.5)	161.1	(40.4)	48.0	22.5
Net DPS (sen)	2.6	3.7	2.1	3.1	3.9
Core FD P/E (x)	25.0	19.0	23.6	15.9	13.0
P/BV (x)	1.5	2.6	1.8	1.7	1.6
Net dividend yield (%)	3.7	2.7	2.0	3.1	3.8
ROAE (%)	5.4	13.1	8.7	12.4	14.3
ROAA (%)	3.6	8.5	5.0	7.4	8.7
EV/EBITDA (x)	11.4	12.2	10.2	7.5	6.0
Net gearing (%) (incl perps)	net cash	1.2	net cash	net cash	net cash
Consensus net profit	-	-	205	323	372
MKE vs. Consensus (%)	-	-	(11.3)	(14.3)	(7.8)

Loh Yan Jin  
 lohyanjin.loh@maybank-ib.com  
 (603) 2297 8687

# HOLD

Share Price	MYR 1.02
12m Price Target	MYR 1.07 (+8%)
Previous Price Target	MYR 1.07

### Company Description

VS Industry Bhd is the 26th largest EMS provider in the world by revenue, ranked according to Manufacturing Market Insider in 2020.

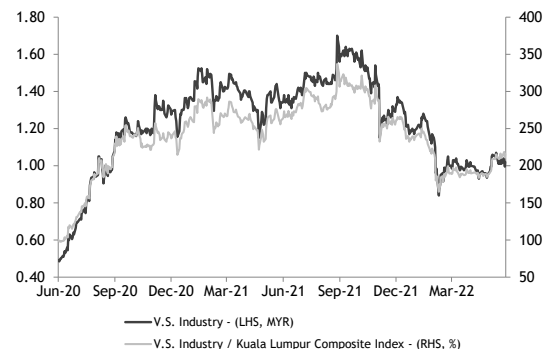
### Statistics

52w high/low (MYR)	1.70/0.84
3m avg turnover (USDm)	1.3
Free float (%)	65.5
Issued shares (m)	3,838
Market capitalisation	MYR3.9B
	USD889M

### Major shareholders:

Kumpulan Wang Persaraan	8.6%
BEH KIM LING	7.7%
BEH HWEE SZE	7.3%

### Price Performance



	-1M	-3M	-12M
Absolute (%)	7	1	(22)
Relative to index (%)	14	12	(16)

Source: FactSet

Figure 1: V.S. Industry results summary

FY Jul (MYR m)	Quarterly results					Cumulative results		
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
Turnover	927.6	1,014.1	(8.5)	1,074.8	(13.7)	2,909.7	3,061.2	(4.9)
EBIT	65.6	56.3	16.6	103.7	(36.7)	174.7	280.4	(37.7)
Interest expense	(2.8)	(2.6)	7.6	(2.3)	23.5	(8.4)	(8.2)	2.3
Interest income	0.4	0.9	(56.7)	0.9	(59.4)	2.2	3.1	(28.8)
Associate	(0.4)	(0.3)	29.7	(2.7)	(84.6)	(1.3)	(2.0)	(33.7)
<b>Pre-tax profit</b>	<b>62.8</b>	<b>54.2</b>	<b>15.8</b>	<b>99.6</b>	<b>(37.0)</b>	<b>167.2</b>	<b>273.3</b>	<b>(38.8)</b>
Taxation	(14.8)	(11.8)	25.7	(27.2)	(45.6)	(39.1)	(73.4)	(46.7)
Minority interest	5.4	0.0	n.m.	1.0	>100	7.0	4.0	76.2
<b>Net profit</b>	<b>53.4</b>	<b>42.4</b>	<b>25.8</b>	<b>73.4</b>	<b>(27.3)</b>	<b>135.2</b>	<b>203.9</b>	<b>(33.7)</b>
E.I.	(0.8)	(0.0)	n.m.	(0.4)	74.2	(1.5)	1.3	n.m.
<b>Core net profit</b>	<b>52.6</b>	<b>42.4</b>	<b>24.0</b>	<b>72.9</b>	<b>(27.9)</b>	<b>133.6</b>	<b>205.2</b>	<b>(34.9)</b>
	3Q22	2Q22	+/- ppt	3Q21	+/- ppt	9M22	9M21	+/- ppt
Core net profit margin (%)	5.7	4.2	1.5	6.8	(1.1)	4.6	6.7	(2.1)
Tax rate (%)	23.6	21.7	1.9	27.3	(3.7)	23.4	26.9	(3.5)
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
<b>Revenue (MYR m)</b>	<b>927.6</b>	<b>1,014.1</b>	<b>(8.5)</b>	<b>1,074.8</b>	<b>(13.7)</b>	<b>2,909.7</b>	<b>3,061.2</b>	<b>(4.9)</b>
Malaysia	825.1	895.6	(7.9)	939.1	(12.1)	2,575.2	2,658.7	(3.1)
Indonesia	83.9	89.1	(5.8)	95.2	(11.9)	252.3	268.7	(6.1)
China	11.5	23.9	(52.0)	37.0	(69.1)	67.3	123.8	(45.7)
Others	7.2	5.6	29.5	3.4	109.0	14.9	9.9	50.2
	3Q22	2Q22	%QoQ	3Q21	%YoY	9M22	9M21	%YoY
<b>Pretax profit (MYR m)</b>	<b>62.8</b>	<b>54.2</b>	<b>15.8</b>	<b>99.6</b>	<b>(37.0)</b>	<b>167.2</b>	<b>273.3</b>	<b>(38.8)</b>
Malaysia	67.7	54.0	25.3	99.7	(32.1)	172.1	271.2	(36.6)
Indonesia	2.4	4.0	(41.3)	2.9	(19.5)	8.5	8.2	4.0
China	(6.5)	(5.5)	18.3	(1.8)	>100	(15.2)	(7.9)	92.9
Others	(0.8)	1.7	n.m.	(1.3)	(40.0)	1.9	1.7	6.4
	3Q22	2Q22	+/- ppt	3Q21	+/- ppt	9M22	9M21	+/- ppt
<b>Pretax profit margins (%)</b>								
Malaysia	6.8	5.3	1.4	9.3	(2.5)	5.7	8.9	(3.2)
Indonesia	8.2	6.0	2.2	10.6	(2.4)	6.7	10.2	(3.5)
China	2.8	4.5	(1.7)	3.1	(0.3)	3.4	3.0	0.3

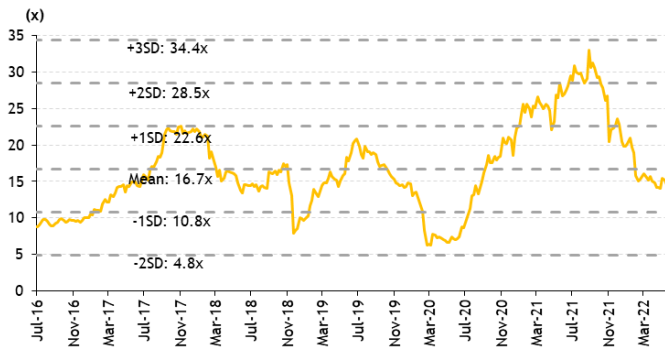
Source: Company, Maybank IBG Research

Figure 2: Revenue forecasts of selected key customers

Customer	Revenue forecasts (MYR'm)		
	FY22E	FY23E	FY24E
UK-based	1,407	1,414	1,415
US-based	987	1,050	1,092
Coffeemaker	748	806	868
Pool cleaner	344	468	558
Customer Y (Home appliances)	200	400	500

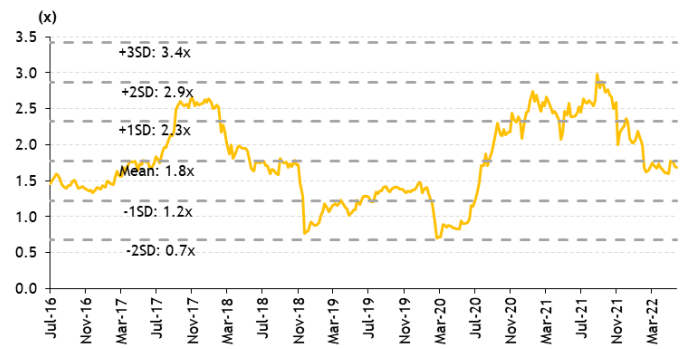
Source: Company, Maybank IBG Research

**Figure 3: VSI's 12M forward PER (currently trades at 14.4x)**



Source: Bloomberg, Maybank IBG Research

**Figure 4: VSI's 12M forward P/BV (currently trades at 1.7x)**



Source: Bloomberg, Maybank IBG Research

### Risk statement

There are several risk factors for our earnings estimates, target price and rating for VSI. Key risks are: (i) weaker-than-expected consumer demand for VSI assembled products (on weakening economics outlook); (ii) lower-than-expected costs pass through (as the mechanism depends on the company's negotiation with its clients); (iii) persistent operational disruptions from labour issues and components shortage; and (iv) USD/MYR forex volatility (we estimate for every +/-1% change in USD/MYR, bottom line impact is +/-0.5%). Potential upside includes (i) better-than-expected revenue from ramped up production (as labour and raw material shortage issue ease); (ii) new customer acquisitions; and (iii) improve margins from better efficiencies due to economics of scales.

FYE 31 Jul	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Metrics</b>					
P/E (reported) (x)	24.3	19.1	21.4	14.0	11.3
Core P/E (x)	24.6	18.7	21.4	14.0	11.3
Core FD P/E (x)	25.0	19.0	23.6	15.9	13.0
P/BV (x)	1.5	2.6	1.8	1.7	1.6
P/NTA (x)	1.5	2.6	1.8	1.7	1.6
Net dividend yield (%)	3.7	2.7	2.0	3.1	3.8
FCF yield (%)	4.7	4.2	5.9	5.5	9.0
EV/EBITDA (x)	11.4	12.2	10.2	7.5	6.0
EV/EBIT (x)	19.2	15.8	15.5	10.0	7.7

**INCOME STATEMENT (MYR m)**

Revenue	3,243.2	4,002.3	4,356.2	4,940.4	5,364.1
EBITDA	226.7	438.6	354.9	470.8	552.0
Depreciation	(89.5)	(99.1)	(118.7)	(116.5)	(114.5)
Amortisation	(2.3)	(2.3)	(2.3)	(2.3)	(2.3)
EBIT	134.9	337.1	233.8	352.0	435.2
Net interest income / (exp)	(10.2)	(7.3)	(14.0)	(11.5)	(8.3)
Associates & JV	2.3	(0.7)	(0.7)	(0.7)	(0.7)
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	126.9	329.1	219.2	339.8	426.2
Income tax	(48.9)	(87.5)	(48.2)	(81.5)	(102.3)
Minorities	12.0	3.7	10.9	18.5	18.6
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	90.0	245.3	181.8	276.7	342.5
Core net profit	104.6	274.3	181.8	276.7	342.5

**BALANCE SHEET (MYR m)**

Cash & Short Term Investments	404.5	402.4	863.0	930.4	1,078.4
Accounts receivable	877.6	992.1	895.1	1,015.2	1,053.2
Inventory	331.8	633.8	409.1	453.9	477.0
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	846.9	989.5	970.8	954.3	939.8
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	364.7	577.8	473.5	467.5	461.5
<b>Total assets</b>	<b>2,825.5</b>	<b>3,595.6</b>	<b>3,611.4</b>	<b>3,821.2</b>	<b>4,010.0</b>
ST interest bearing debt	215.4	318.8	318.8	318.8	318.8
Accounts payable	576.0	844.2	767.3	838.2	879.6
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	47.0	109.4	109.4	109.4	80.4
Other liabilities	118.0	106.0	106.0	106.0	106.0
<b>Total Liabilities</b>	<b>956.7</b>	<b>1,378.1</b>	<b>1,301.3</b>	<b>1,372.2</b>	<b>1,384.6</b>
Shareholders Equity	1,702.4	2,040.5	2,144.0	2,301.4	2,496.3
Minority Interest	166.4	177.0	166.1	147.7	129.1
<b>Total shareholder equity</b>	<b>1,868.8</b>	<b>2,217.5</b>	<b>2,310.1</b>	<b>2,449.1</b>	<b>2,625.4</b>
<b>Total liabilities and equity</b>	<b>2,825.5</b>	<b>3,595.6</b>	<b>3,611.4</b>	<b>3,821.2</b>	<b>4,010.0</b>

**CASH FLOW (MYR m)**

Pretax profit	126.9	329.1	219.2	339.8	426.2
Depreciation & amortisation	91.8	101.5	121.1	118.8	116.8
Adj net interest (income)/exp	10.2	7.3	14.0	11.5	8.3
Change in working capital	79.0	(266.9)	23.7	(77.4)	(1.8)
Cash taxes paid	(48.9)	(87.5)	(48.2)	(81.5)	(102.3)
Other operating cash flow	(31.2)	358.5	0.7	0.7	0.7
Cash flow from operations	227.9	442.1	330.4	311.8	447.9
Capex	(107.2)	(227.3)	(100.0)	(100.0)	(100.0)
Free cash flow	120.7	214.8	230.4	211.8	347.9
Dividends paid	(48.1)	(105.7)	(78.4)	(119.3)	(147.6)
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Change in Debt	5.1	19.2	0.0	0.0	(29.0)
Other invest/financing cash flow	(19.0)	(18.1)	(25.2)	(25.2)	(23.3)
Effect of exch rate changes	21.9	19.1	0.0	0.0	0.0
Net cash flow	80.7	129.2	126.8	67.4	148.1

FYE 31 Jul	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	(18.5)	23.4	8.8	13.4	8.6
EBITDA growth	(25.0)	93.5	(19.1)	32.7	17.3
EBIT growth	(33.6)	149.9	(30.6)	50.5	23.6
Pretax growth	(30.2)	159.3	(33.4)	55.0	25.4
Reported net profit growth	(45.6)	172.5	(25.9)	52.2	23.8
Core net profit growth	(46.6)	162.2	(33.7)	52.2	23.8
<b>Profitability ratios (%)</b>					
EBITDA margin	7.0	11.0	8.1	9.5	10.3
EBIT margin	4.2	8.4	5.4	7.1	8.1
Pretax profit margin	3.9	8.2	5.0	6.9	7.9
Payout ratio	106.8	56.2	43.1	43.1	43.1
<b>DuPont analysis</b>					
Net profit margin (%)	2.8	6.1	4.2	5.6	6.4
Revenue/Assets (x)	1.1	1.1	1.2	1.3	1.3
Assets/Equity (x)	1.7	1.8	1.7	1.7	1.6
ROAE (%)	5.4	13.1	8.7	12.4	14.3
ROAA (%)	3.6	8.5	5.0	7.4	8.7
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	68.2	60.5	51.9	38.9	39.0
Days receivable outstanding	103.9	84.1	78.0	69.6	69.4
Days inventory outstanding	43.3	50.0	47.8	35.6	35.9
Days payables outstanding	79.1	73.6	73.8	66.3	66.3
Dividend cover (x)	0.9	1.8	2.3	2.3	2.3
Current ratio (x)	2.0	1.9	2.0	2.1	2.2
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	3.0	2.6	2.8	2.8	2.9
Net gearing (%) (incl perps)	net cash	1.2	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	1.2	net cash	net cash	net cash
Net interest cover (x)	13.2	46.0	16.7	30.5	52.2
Debt/EBITDA (x)	1.2	1.0	1.2	0.9	0.7
Capex/revenue (%)	3.3	5.7	2.3	2.0	1.9
Net debt/ (net cash)	(142.1)	25.8	(434.8)	(502.2)	(679.3)

Source: Company; Maybank IBG Research

## Research Offices

### ECONOMICS

**Suhaimi ILIAS**  
Chief Economist  
Malaysia | Philippines | Global  
(603) 2297 8682  
suhaimi\_ilias@maybank-ib.com

**CHUA Hak Bin**  
Regional Thematic Macroeconomist  
(65) 6231 5830  
chuahb@maybank.com

**LEE Ju Ye**  
Singapore | Thailand | Indonesia  
(65) 6231 5844  
leejuye@maybank.com

**Dr Zamros DZULKAFLI**  
(603) 2082 6818  
zamros.d@maybank-ib.com

**Fatin Nabila MOHD ZAINI**  
(603) 2297 8685  
fatinnabila.mohdzaini@maybank-ib.com

**Brian LEE Shun Rong**  
(65) 6231 5846  
brian.lee1@maybank.com

**Luong Thu Huong**  
(65) 62315 8467  
hana.thuluong@maybank.com

### FX

**Saktiandi SUPAAT**  
Head of FX Research  
(65) 6320 1379  
saktiandi@maybank.com.sg

**Christopher WONG**  
(65) 6320 1347  
wongkl@maybank.com.sg

**TAN Yanxi**  
(65) 6320 1378  
tanyx@maybank.com.sg

**Fiona LIM**  
(65) 6320 1374  
fionallim@maybank.com.sg

### STRATEGY

**Anand PATHMAKANTHAN**  
ASEAN  
(603) 2297 8783  
anand.pathmakanthan@maybank-ib.com

### FIXED INCOME

**Winson PHOON, FCA**  
(65) 6340 1079  
winsonphoon@maybank.com

**SE THO Mun Yi, CFA**  
(603) 2074 7606  
munyi.st@maybank-ib.com

### REGIONAL EQUITIES

**Anand PATHMAKANTHAN**  
Head of Regional Equity Research  
(603) 2297 8783  
anand.pathmakanthan@maybank-ib.com

**WONG Chew Hann, CA**  
Head of ASEAN Equity Research  
(603) 2297 8686  
wchewh@maybank-ib.com

**ONG Seng Yeow**  
Research, Technology & Innovation  
(65) 6231 5839  
ongsengyeow@maybank.com

### MALAYSIA

**Anand PATHMAKANTHAN** *Head of Research*  
(603) 2297 8783  
anand.pathmakanthan@maybank-ib.com  
• Strategy

**WONG Chew Hann, CA**  
(603) 2297 8686  
wchewh@maybank-ib.com  
• Non-Bank Financials (stock exchange)  
• Construction & Infrastructure

**Desmond CH'NG, BFP, FCA**  
(603) 2297 8680  
desmond.chng@maybank-ib.com  
• Banking & Finance

**LIAW Thong Jung**  
(603) 2297 8688 tjliaw@maybank-ib.com  
• Oil & Gas Services- Regional  
• Automotive

**ONG Chee Ting, CA**  
(603) 2297 8678 ct.ong@maybank-ib.com  
• Plantations - Regional

**YIN Shao Yang, CPA**  
(603) 2297 8916 samuel.y@maybank-ib.com  
• Gaming - Regional  
• Media • Aviation • Non-Bank Financials

**TAN Chi Wei, CFA**  
(603) 2297 8690 chiwei.t@maybank-ib.com  
• Power • Telcos

**WONG Wei Sum, CFA**  
(603) 2297 8679 weisum@maybank-ib.com  
• Property • Glove

**Jade TAM**  
(603) 2297 8687 jade.tam@maybank-ib.com  
• Consumer Staples & Discretionary

**Nur Farah SYIFAA**  
(603) 2297 8675  
nurfarahsyifaa.mohamadfuad@maybank-ib.com  
• Construction • Renewable Energy • REITs

**Arvind JAYARATNAM**  
(603) 2297 8692  
arvind.jayaratnam@maybank.com  
• Petrochemicals • Technology

**Shafiq KADIR**  
(603) 2297 8691  
msshafiqk.abkadir@maybank-ib.com  
• Healthcare • Software

**LOH Yan Jin**  
(603) 2297 8687  
lohyanjin.loh@maybank-ib.com  
• Ports • Shipping

**TEE Sze Chiah** *Head of Retail Research*  
(603) 2082 6858 szechiah.t@maybank-ib.com  
• Retail Research

**Nik Ihsan RAJA ABDULLAH, MSTA, CFTe**  
(603) 2297 8694  
nikmohdihsan.ra@maybank-ib.com  
• Chartist

**Amirah AZMI**  
(603) 2082 8769 amirah.azmi@maybank-ib.com  
• Retail Research

### SINGAPORE

**Thilan WICKRAMASINGHE** *Head of Research*  
(65) 6231 5840 thilanw@maybank.com  
• Banking & Finance - Regional  
• Consumer

**CHUA Su Tye**  
(65) 6231 5842 chuasutye@maybank.com  
• REITs - Regional

**LAI Gene Lih, CFA**  
(65) 6231 5832 laigenelih@maybank.com  
• Technology

**Eric ONG**  
(65) 6231 5924 ericong@maybank.com  
• Healthcare • Transport • SMIDs

**Kelvin TAN**  
(65) 6231 5837 kelvintan1@maybank.com  
• Telcos • Industrials

**Samuel TAN**  
(65) 6231 5843 samuel.tan@maybank.com  
• Technology

**LI Jialin**  
(65) 6231 5845 jialin.li@maybank.com  
• REITs

### PHILIPPINES

**Jacqui de JESUS** *Head of Research*  
(63) 2 8849 8840  
jacqui.dejesus@maybank.com  
• Strategy • Conglomerates

**Rachelleen RODRIGUEZ, CFA**  
(63) 2 8849 8843  
rachelleen.rodriguez@maybank.com  
• Banking & Finance • Transport • Telcos

**Daphne SZE**  
(63) 2 8849 8847  
daphne.sze@maybank.com  
• Consumer

**Miguel SEVIDAL**  
(63) 2 8849 8844  
miguel.sevidal@maybank.com  
• REITs • Property

**Fiorenzo de JESUS**  
(63) 2 8849 8846  
fiorenzo.dejesus@maybank.com  
• Utilities

### VIETNAM

**Quan Trong Thanh** *Head of Research*  
(84 28) 44 555 888 ext 8184  
thanh.quan@maybank.com  
• Banks

**Hoang Huy, CFA**  
(84 28) 44 555 888 ext 8181  
hoanghuy@maybank.com  
• Strategy • Technology • Industrials

**Le Nguyen Nhat Chuyen**  
(84 28) 44 555 888 ext 8082  
chuyen.le@maybank.com  
• Oil & Gas • Logistics

**Nguyen Thi Sony Tra Mi**  
(84 28) 44 555 888 ext 8084  
trami.nguyen@maybank.com  
• Consumer

**Tyler Manh Dung Nguyen**  
(84 28) 44 555 888 ext 8085  
manhdung.nguyen@maybank.com  
• Utilities • Property

**Tran Thi Thanh Nhan**  
(84 28) 44 555 888 ext 8088  
nhan.tran@maybank.com  
• Consumer

**Nguyen Thi Ngan Tuyen**  
*Head of Retail Research*  
(84 28) 44 555 888 ext 8081  
tuyen.nguyen@maybank.com  
• Retail Research

**Nguyen Thanh Lam**  
(84 28) 44 555 888 ext 8086  
thanhlam.nguyen@maybank.com  
• Chartist

### INDIA

**Jigar SHAH** *Head of Research*  
(91) 22 4223 2632 jigars@maybank.com  
• Strategy • Oil & Gas • Automobile • Cement

**Neerav DALAL**  
(91) 22 4223 2606 neerav@maybank.com  
• Software Technology • Telcos

**Vikram RAMALINGAM**  
(91) 22 4223 2607  
vikram@maybank.com  
• Automobile • Media

### INDONESIA

**Rahmi MARINA**  
(62) 21 8066 8689  
rahmi.marina@maybank.com  
• Banking & Finance

**Willy GOUTAMA**  
(62) 21 8066 8500  
willygoutama@maybank.com  
• Consumer

**Satriawan, CTA**  
(62) 21 8066 8682  
satriawan@maybank.com  
• Chartist

### THAILAND

**Jesada TECHAHUSDIN, CFA**  
(66) 2658 6300 ext 1395  
jesada.t@maybank.com  
• Banking & Finance

**Vanida GEISLER, CPA**  
(66) 2658 6300 ext 1394  
Vanida.G@maybank.com  
• Property • REITs

**Yuwanee PROMMAPORN**  
(66) 2658 6300 ext 1393  
Yuwanee.P@maybank.com  
• Services • Healthcare

**Wasu MATTANAPOTCHANART**  
(66) 2658 6300 ext 1392  
wasu.m@maybank.com  
• Telcos

**Surachai PRAMUALCHAROENKIT**  
(66) 2658 5000 ext 1470  
Surachai.p@maybank.com  
• Auto • Conmat • Contractor • Steel

**Suttatip PEERASUB**  
(66) 2658 5000 ext 1430  
suttatip.p@maybank.com  
• Food & Beverage • Commerce

**Jaroonpan WATTANAWONG**  
(66) 2658 5000 ext 1404  
jaroonpan.w@maybank.com  
• Transportation • Small cap

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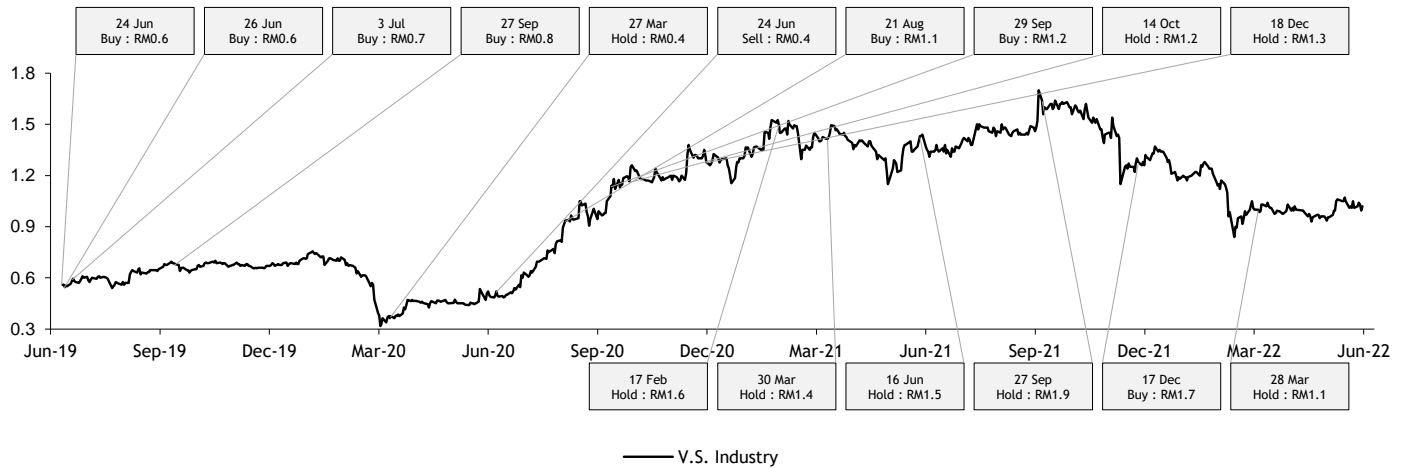
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### Malaysia

Maybank Investment Bank Berhad  
(A Participating Organisation of  
Bursa Malaysia Securities Berhad)  
33rd Floor, Menara Maybank,  
100 Jalan Tun Perak,  
50050 Kuala Lumpur  
Tel: (603) 2059 1888;  
Fax: (603) 2078 4194  
Stockbroking Business:  
Level 8, Tower C, Dataran Maybank,  
No.1, Jalan Maarof  
59000 Kuala Lumpur  
Tel: (603) 2297 8888  
Fax: (603) 2282 5136

### Singapore

Maybank Securities Pte Ltd  
Maybank Research Pte Ltd  
50 North Canal Road  
Singapore 059304

Tel: (65) 6336 9090

### Hong Kong

MIB Securities (Hong Kong) Limited  
28/F, Lee Garden Three,  
1 Sunning Road, Causeway Bay,  
Hong Kong

Tel: (852) 2268 0800  
Fax: (852) 2877 0104

### London

Maybank Securities (London) Ltd  
PNB House  
77 Queen Victoria Street  
London EC4V 4AY, UK

Tel: (44) 20 7332 0221  
Fax: (44) 20 7332 0302

### Indonesia

PT Maybank Sekuritas Indonesia  
Sentral Senayan III, 22<sup>nd</sup> Floor  
Jl. Asia Afrika No. 8  
Gelora Bung Karno, Senayan  
Jakarta 10270, Indonesia

Tel: (62) 21 2557 1188  
Fax: (62) 21 2557 1189

### New York

Maybank Securities USA Inc  
400 Park Avenue, 11th Floor  
New York, New York 10022,  
U.S.A.

Tel: (212) 688 8886  
Fax: (212) 688 3500

### India

MIB Securities India Pte Ltd  
1101, 11<sup>th</sup> floor, A Wing, Kanakia  
Wall Street, Chakala, Andheri -  
Kurla Road, Andheri East,  
Mumbai City - 400 093, India

Tel: (91) 22 6623 2600  
Fax: (91) 22 6623 2604

### Philippines

Maybank Securities Inc  
17/F, Tower One & Exchange Plaza  
Ayala Triangle, Ayala Avenue  
Makati City, Philippines 1200

Tel: (63) 2 8849 8888  
Fax: (63) 2 8848 5738

### Thailand

Maybank Securities (Thailand) PCL  
999/9 The Offices at Central World,  
20<sup>th</sup> - 21<sup>st</sup> Floor,  
Rama 1 Road Pathumwan,  
Bangkok 10330, Thailand

Tel: (66) 2 658 6817 (sales)  
Tel: (66) 2 658 6801 (research)

### Vietnam

Maybank Securities Limited  
4A-15+16 Floor Vincom Center Dong  
Khoi, 72 Le Thanh Ton St. District 1  
Ho Chi Minh City, Vietnam

Tel : (84) 844 555 888  
Fax : (84) 8 38 271 030

### Sales Trading

Kevin Foy  
Regional Head Sales Trading  
kevinfoy@maybank.com  
Tel: (65) 6636-3620  
US Toll Free: 1-866-406-7447

#### Indonesia

Helen Widjaja  
helen.widjaja@maybank.com  
(62) 21 2557 1188

#### New York

James Lynch  
jlynch@maybank-keusa.com  
Tel: (212) 688 8886

#### Philippines

Keith Roy  
keith\_roy@maybank.com  
Tel: (63) 2 848-5288

#### London

Greg Smith  
gsmith@maybank.co.uk  
Tel: (44) 207-332-0221

#### India

Sanjay Makhija  
sanjaymakhija@maybank.com  
Tel: (91)-22-6623-2629