

## Capital A (CAPITALA MK)

# AirAsia Cambodia a potential beneficiary of Belt & Road?

### Maintain BUY call and MYR0.84 SOP-based TP

CAPITALA has proposed to set up a 51%-owned JV in Cambodia, AirAsia Cambodia (AAC). We are unsure if it will be profitable right away but note that Cambodian-Chinese relations are close as exemplified by the many Belt & Road investments in Cambodia. AAC could capitalise on that relationship. Perhaps that is why AAC is slated to commence operations in late-2023, when many believe China will reopen its borders. Maintain earnings estimates, BUY call and MYR0.84 SOP-based TP for now.

### To venture into Cambodia via 51%-owned JV

CAPITALA/Sivilai Asia (Not Listed) plans to invest 51%/49% of the issued and paid-up capital (PUC) of a Cambodian JV to be incorporated as AirAsia (Cambodia) Co. Ltd. (AAC). If approved, AAC will operate as a low cost carrier based in Cambodia. CAPITALA will also execute a Brand License Agreement with AAC in return for a fee. AAC is expected to commence operations in late 2023 with 2 A321s and eventually expand to 15 A321s. A321s can accommodate 236 passengers and fly  $\leq 6,000$  km.

### Initial investment small; profitable right away?

The fully PUC of AAC is anticipated to be  $\geq$ USD25m (CAPITALA share: USD12.8m). The initial capital will be USD5m (CAPITALA share: USD2.6m) and will be injected in 3 tranches from the present day until a month before operations commence. Given the small initial capital, we do not foresee this JV negatively impacting CAPITALA's cash flows. CAPITALA CEO, Tony Fernandes was quoted as saying that AAC will generate profits in its first year of operations.

### Maintain earnings estimates for now

Yet, Mr. Fernandes statement is not without merit. **One**, staff costs in Cambodia is low even by ASEAN standards. **Two**, lease rates for A321s are 5-15% cheaper relative to pre-COVID (Fig. 1). **Third**, there is not much competition from other Cambodian airlines. Cambodian airlines operate only 20 aircraft (Fig. 2). **Four**, there is a large Chinese diaspora in Cambodia working in Belt & Road projects and textiles. In 2019, there were c.500 China-Cambodia flights weekly (China-Malaysia: 389).

FYE Dec (MYR m)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	3,274	1,836	7,349	13,402	16,409
EBITDAR	(1,492)	(967)	(253)	2,427	3,330
Core net profit	(3,484)	(2,759)	(2,890)	(700)	258
Core FDEPS (sen)	(104.2)	(72.9)	(47.0)	(10.6)	5.4
Core FDEPS growth(%)	nm	nm	nm	nm	nm
Net DPS (sen)	0.0	0.0	0.0	0.0	0.0
Core FD P/E (x)	nm	nm	nm	nm	11.1
P/BV (x)	nm	nm	nm	nm	nm
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
ROAE (%)	(71.7)	(89.8)	(376.6)	76.2	(22.6)
ROAA (%)	(15.3)	(13.8)	(14.8)	(3.8)	1.5
EV/EBITDAR (x)	nm	nm	nm	9.7	6.0
Net gearing (%) (incl perps)	nm	nm	nm	nm	nm
Consensus net profit	-	-	(2,700)	(276)	368
MKE vs. Consensus (%)	-	-	(5.5)	(154.1)	(29.9)

Yin Shao Yang  
samuel.y@maybank-ib.com  
(603) 2297 8916

# BUY

Share Price	MYR 0.60
12m Price Target	MYR 0.84 (+41%)
Previous Price Target	MYR 0.84

### Company Description

*AirAsia Group is Asia's foremost low cost carrier with operations in Malaysia, Thailand, Indonesia and Philippines.*

### Statistics

52w high/low (MYR)	0.83/0.55
3m avg turnover (USDm)	0.6
Free float (%)	49.5
Issued shares (m)	4,162
Market capitalisation	MYR2.5B USD562M

### Major shareholders:

Tune Air Sdn Bhd	12.4%
Tune Live Sdn. Bhd.	12.2%
Positive Boom Ltd.	8.0%

### Price Performance



— Capital A - (LHS, MYR) — Capital A / Kuala Lumpur Composite Index - (RHS, %)

	-1M	-3M	-12M
Absolute (%)	3	(8)	(24)
Relative to index (%)	0	(7)	(23)

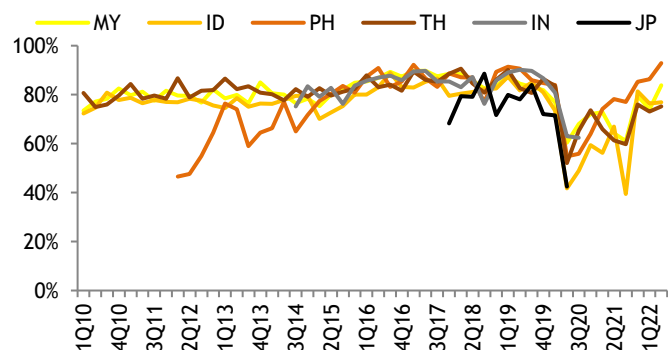
Source: FactSet

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## Value Proposition

- Asia's leading low cost carrier with highest market share, largest fleet size and most extensive route network.
- Operates in 4 countries after exiting Japan and India, which provides unrivalled route network reach.
- Lowest unit cost airline in the world. Management is very ambitious, cost conscious and forward-thinking.
- Growing middle class in Asia fuelling growth in demand for air travel.
- Won the coveted 'World's Best LCC' award for a record 13 times in a row by Skytrax.

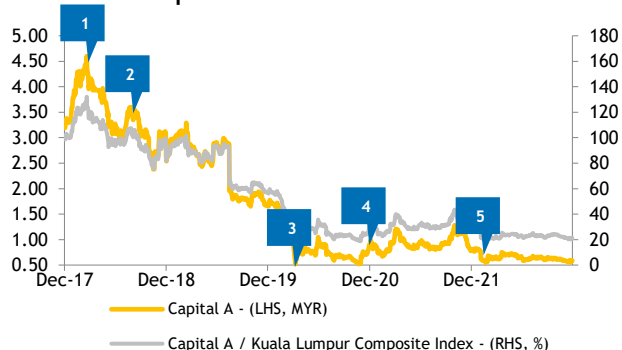
### AirAsia passengers load factor by country



Source: Company

## Price Drivers

### Historical share price trend



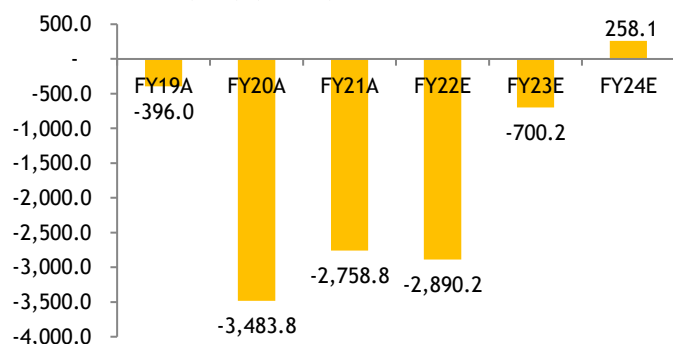
Source: Company, Maybank IBG Research

1. CAPITALA announced record dividends which provided a catalyst to its share price.
2. Market de-rated following the outcome of the 14<sup>th</sup> General Election (May 2018).
3. COVID-19 pandemic struck Malaysia. CAPITALA grounded most of its fleet in late-Mar 2020.
4. Pfizer, Moderna and AstraZeneca announced that they have developed effective COVID-19 vaccines.
5. CAPITALA classified as a PN17 listed issuer by Bursa Malaysia.

## Financial Metrics

- Best financial indicator is core net profit ex disposal gains, forex and fair value changes, and deferred taxation.
- Still forecast FY22E/FY23E core net loss as passengers carried will be limited by measured aircraft redeployment.
- Forecast FY24E to generate net profit on passengers carried recovering and average fares rising.
- Sensitive to fuel price movement, a USD1 per barrel change in fuel price will move earnings by MYR10m-MYR30m.
- Balance sheet as at end-4Q21 in a net debt position of MYR1.11b if ex-finance lease liabilities.

### Core net profit/(loss) (MYRm)



Source: Company (historical), Maybank IBG Research (forecasts)

## Swing Factors

### Upside

- Policy changes - visa requirement relaxations and tourist friendly events drive passenger traffic growth.
- Less competition - COVID-19 pandemic has caused competitors to reduce capacity and raise prices.
- Financial assistance - will enable CAPITALA to fill temporary liquidity gaps and survive.

### Downside

- Exogenous events - SARS; MH370, MH17 & AK8501 tragedies; and COVID-19 negatively impacted passenger traffic growth.
- Fuel prices - they are volatile and there is no certainty that they will be hedged at low levels.
- Weak MYR - 60-70% of operating costs are USD denominated.

# ESG@MAYBANK IBG

samuel.y@maybank-ib.com

Risk Rating & Score <sup>1</sup>	32.1 (High)
Score Momentum <sup>2</sup>	-3.3
Last Updated	16 Mar 2022
Controversy Score <sup>3</sup> (Updated: 4 Feb 2022)	2 - Customer Incidents, Business Ethics Incidents, Governance Incidents

## Business Model & Industry Issues

- Being an airline, CAPITALA may not be deemed as environmentally friendly but it operates Airbus A320 family aircraft which are already fuel efficient. It will gradually replace its entire fleet with the even more fuel efficient A321neo aircraft.
- As at end-FY21, only 35% of staff are female but this is not entirely unexpected as operational functions (e.g. engineering) tend to be filled by males.
- An especially positive point is that CAPITALA supported staff that were laid off during the COVID-19 pandemic and even established an academy to retrain staff in technology and IT.
- To be sure, some senior managers have made headlines for the wrong reasons but to be fair, no misconduct has been proven to date. However, CAPITALA's decision to enter and exit Japan twice raised eyebrows.
- In all, we rate CAPITALA's ESG credentials as moderate. CAPITALA was included in the FTSE4GOOD Bursa Malaysia Index in Dec 2020.

## Material E issues

- As at end-FY21, operated 168 Airbus A320, 40 Airbus A320neo, 4 Airbus A321neo and 1 Airbus A330ceo.
- Will gradually replace entire fleet with Airbus A321neo which is 10-15% more fuel efficient than the Airbus A320.
- Carbon intensity ratio (CIR) was up 7% YoY to 94gCO<sub>2</sub>/RPK in FY21 due to less RPK flown.
- Fuel consumption/100RPK was up 7% YoY to 3.78 litres in FY21 due to shorter stage lengths.
- CIR and fuel efficiency to normalise as RPK and stage length recover due to the COVID-19 pandemic easing.
- Targets carbon neutral growth (relative to 2019 as the base line year) and net zero CO<sub>2</sub> emissions by 2050.
- Plans to incorporate sustainable aviation fuel and introduce carbon offsetting options.
- Partners TRAFFIC to raise awareness of illegal wildlife trafficking in the aviation sector.

## Material S issues

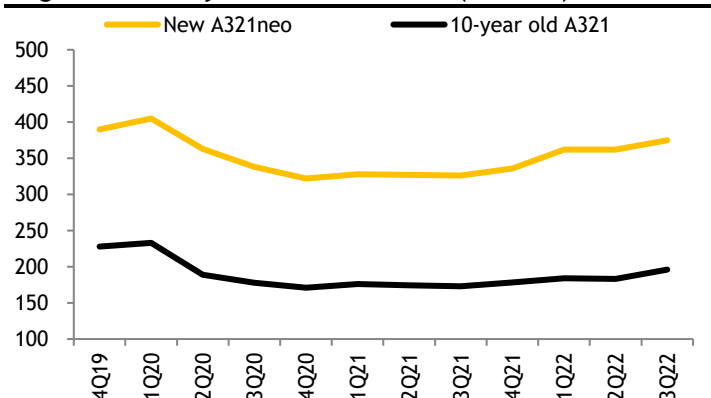
- Trained 71% of staff on-line to recognise the signs of human trafficking on board and respond appropriately.
- Hosted its first international webinar, "The Role of Airline Staff as Frontliners in the Fight Against Human Trafficking" and joined ICAO's Anti-Trafficking Working Group.
- Flew 410 rescue and repatriation flights to bring >15,000 individuals home in FY20.
- MYR10.5m spent on training staff in FY21 (-22% YoY) despite the group having generated a huge net loss.
- Launched Redbeat Academy in Oct 2020 to retrain staff in technology and IT.
- As at end-FY21, only 35% of staff is female. Skewed by males in operational functions (e.g. engineering).
- Through AirAsia Foundation, supported 28 social enterprises benefitting >10,000 individuals as at end-FY21.

## Key G metrics and issues

- BOD comprises Non-Independent Executive Chairman (NIEC), Non-Independent Executive Director & Chief Executive Officer (NIED & CEO), Non-Independent Non-Executive Director (NINED) and 3 Independent Non-Executive Directors (INED). Independent Directors made up 50% of its BOD size, meeting the minimum of Malaysian Code on Corporate Governance's recommendation.
- Only 1 of the 6 BOD members is a woman, Surina Binti Shukri, short of the 30% recommendation. She is an INED.
- Major shareholders, Tune Air and Tune Live are represented on the BOD by the NIEC and NIED & CEO.
- There are 3 BOD committees (i.e. Audit, Nomination & Remuneration and Risk Management).
- The Audit and Nomination & Remuneration Committees are chaired by INEDs.
- The Risk Management Committee, however, is chaired by the NINED.
- FY21 directors' remuneration surged 170% YoY despite generating heavy losses still.
- Ernst & Young PLT is the independent auditor since 2017. The predecessor was PricewaterhouseCoopers PLT.
- Fined by Malaysian Aviation Commission for charging processing fees in FY19 and FY20 (MYR2.2m total) and advertising misleading airfares in FY18 (MYR160k).
- Fined by Malaysia Competition Commission for entering into a collaboration agreement with Malaysia Airlines (MYR10m) in FY14.
- India's Central Bureau of Investigation (CBI) filed a case against the NIED & CEO over alleged violation of norms in getting international flying licenses in FY18.
- The NIED & CEO has not responded to the CBI's case to date.
- The NIEC and NIED & CEO were implicated in a bribery case involving Airbus in FY20. Both were later cleared.
- Ventured into Japan twice. AirAsia Japan consumed >MYR400m in investments but never generated an annual profit. AirAsia Japan filed for bankruptcy in Oct 2020.

<sup>1</sup>**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. <sup>2</sup>**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. <sup>3</sup>**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Figure 1: Monthly lease rates of A321s (USD'000)



Source: IBA

Figure 2: Fleet profile of Cambodian airlines

Airline	ATR72	A319	A320	A321
Bassaka Air	-	-	2	-
Cambodia Angkor Air	2	-	2	1
Cambodia Airways	-	3	3	-
JC International Airlines	-	-	1	-
Lanmei Airlines	-	-	2	2
Sky Angkor Airlines	-	-	1	1
<b>Total</b>	<b>2</b>	<b>3</b>	<b>11</b>	<b>4</b>

Source: planespotters.net

Figure 3: CAPITALA valuation

	FY24E	PER (X)	Value	Value/shr	Comment
Airline net profit with RCUIDS interest expenses added back	447.8	8.0	3,582.6	0.60	
AirAsia X			-	-	assume nil
Tune Protect Group			29.8	0.00	14% of market capitalisation
Proceeds from warrants			649.7	0.11	MYR1.00 exercise price
Proceeds from ESOS			112.6	0.02	MYR0.743 exercise price
<b>Aviation business (A)</b>			<b>4,374.6</b>	<b>0.73</b>	
airasia SuperApp			4,328.6	0.72	96% of USD1.0b valuation
Teleport			1,333.5	0.22	99% of USD300m valuation
<b>Digital business (B)</b>			<b>5,662.1</b>	<b>0.94</b>	
<b>Total (C=A+B)</b>			<b>10,036.7</b>	<b>1.67</b>	
(50% discount) (D=CX-50%)			-5,018.3	-0.84	
<b>SOP (E=C+D)</b>			<b>5,018.3</b>	<b>0.84</b>	

Source: Maybank Investment Banking Group

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Metrics</b>					
P/E (reported) (x)	nm	nm	nm	nm	9.6
Core P/E (x)	nm	nm	nm	nm	9.6
Core FD P/E (x)	nm	nm	nm	nm	11.1
P/BV (x)	nm	nm	nm	nm	nm
P/NTA (x)	(1.6)	(0.7)	(0.4)	(0.3)	(0.3)
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
FCF yield (%)	nm	nm	nm	27.1	52.7
EV/EBITDAR (x)	nm	nm	nm	9.7	6.0
EV/EBIT (x)	nm	nm	nm	28.6	11.7

**INCOME STATEMENT (MYR m)**

Revenue	3,274.4	1,836.2	7,349.0	13,402.2	16,409.3
EBITDAR	(1,491.8)	(967.2)	(253.0)	2,426.9	3,329.7
Depreciation	(2,073.0)	(1,820.6)	(1,573.8)	(1,605.8)	(1,605.8)
EBIT	(3,564.8)	(2,816.6)	(1,826.7)	821.1	1,723.9
Net interest income / (exp)	(597.7)	(644.5)	(976.1)	(1,052.9)	(1,018.6)
Associates & JV	(63.5)	(45.2)	(523.6)	(139.0)	(70.9)
Exceptionals	(1,325.2)	(68.7)	40.7	0.0	0.0
Pretax profit	(5,551.3)	(3,575.0)	(3,285.7)	(370.8)	634.4
Income tax	(17.8)	(5.0)	(4.6)	(4.6)	(4.6)
Minorities	776.3	729.7	440.8	(324.8)	(371.7)
Reported net profit	(5,111.7)	(2,991.1)	(2,849.5)	(700.2)	258.1
Core net profit	(3,483.8)	(2,758.8)	(2,890.2)	(700.2)	258.1

**BALANCE SHEET (MYR m)**

Cash & Short Term Investments	533.3	1,256.8	1,144.9	1,727.3	2,934.4
Accounts receivable	1,537.7	832.5	649.4	649.4	649.4
Inventory	141.4	153.6	153.6	153.6	153.6
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	1,085.6	933.5	818.8	704.1	589.4
Intangible assets	640.6	833.5	833.5	833.5	833.5
Investment in Associates & JVs	484.1	438.9	675.2	536.3	465.4
Other assets	15,443.1	15,581.2	14,622.9	13,156.8	11,674.6
<b>Total assets</b>	<b>19,865.8</b>	<b>20,029.9</b>	<b>18,898.3</b>	<b>17,760.9</b>	<b>17,300.3</b>
ST interest bearing debt	4,263.5	4,793.0	3,854.6	4,189.6	4,392.4
Accounts payable	2,508.9	2,308.9	2,308.9	2,308.9	2,308.9
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	9,460.7	11,812.2	14,719.7	13,629.4	12,336.2
Other liabilities	7,203.0	7,539.0	7,530.0	7,524.0	7,524.0
<b>Total Liabilities</b>	<b>23,435.6</b>	<b>26,452.8</b>	<b>28,413.7</b>	<b>27,651.7</b>	<b>26,561.3</b>
Shareholders Equity	(1,214.3)	(3,382.3)	(6,034.0)	(6,734.2)	(6,476.0)
Minority Interest	(2,355.5)	(3,040.6)	(3,481.4)	(3,156.6)	(2,785.0)
<b>Total shareholder equity</b>	<b>(3,569.8)</b>	<b>(6,422.9)</b>	<b>(9,515.4)</b>	<b>(9,890.8)</b>	<b>(9,261.0)</b>
<b>Total liabilities and equity</b>	<b>19,865.8</b>	<b>20,029.9</b>	<b>18,898.3</b>	<b>17,760.9</b>	<b>17,300.3</b>

**CASH FLOW (MYR m)**

Pretax profit	(5,551.3)	(3,575.0)	(3,285.7)	(370.8)	634.4
Depreciation & amortisation	2,073.0	1,820.6	1,573.8	1,605.8	1,605.8
Adj net interest (income)/exp	549.9	552.0	726.2	726.6	692.4
Change in working capital	(800.3)	209.2	(10.5)	(33.8)	(33.8)
Cash taxes paid	(25.3)	(4.6)	(12.9)	(11.2)	(4.6)
Other operating cash flow	1,585.7	320.1	482.9	139.0	70.9
Cash flow from operations	(2,168.2)	(677.7)	(526.2)	2,055.6	2,965.0
Capex	(100.5)	(50.1)	(50.0)	(50.0)	(50.0)
Free cash flow	(3,148.9)	(1,151.6)	(1,367.3)	671.9	1,304.5
Dividends paid	0.0	0.0	0.0	0.0	0.0
Equity raised / (purchased)	0.0	336.5	0.0	0.0	0.0
Change in Debt	(412.5)	733.9	340.0	(1,448.2)	(1,748.9)
Other invest/financing cash flow	589.8	431.3	124.3	25.1	41.0
Effect of exch rate changes	65.0	(69.7)	0.0	0.0	0.0
Net cash flow	(2,026.4)	704.1	(111.9)	582.4	1,207.2

FYE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	(72.4)	(43.9)	300.2	82.4	22.4
EBITDAR growth	nm	nm	nm	nm	37.2
EBIT growth	nm	nm	nm	nm	110.0
Pretax growth	nm	nm	nm	nm	nm
Reported net profit growth	nm	nm	nm	nm	nm
Core net profit growth	nm	nm	nm	nm	nm
<b>Profitability ratios (%)</b>					
EBITDAR margin	nm	nm	nm	18.1	20.3
EBIT margin	nm	nm	nm	6.1	10.5
Pretax profit margin	nm	nm	nm	nm	3.9
Payout ratio	0.0	0.0	0.0	0.0	0.0
<b>DuPont analysis</b>					
Net profit margin (%)	nm	nm	nm	nm	1.6
Revenue/Assets (x)	0.2	0.1	0.4	0.8	0.9
Assets/Equity (x)	nm	nm	nm	nm	nm
ROAE (%)	(71.7)	(89.8)	(376.6)	76.2	(22.6)
ROAA (%)	(15.3)	(13.8)	(14.8)	(3.8)	1.5
<b>Liquidity &amp; Efficiency</b>					
Dividend cover (x)	nm	nm	nm	nm	nm
Current ratio (x)	0.3	0.3	0.3	0.3	0.4
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	0.8	0.8	0.7	0.6	0.7
Net gearing (%) (incl perps)	nm	nm	nm	nm	nm
Net gearing (%) (excl. perps)	nm	nm	nm	nm	nm
Net interest cover (x)	na	na	na	0.8	1.7
Debt/EBITDAR (x)	nm	nm	nm	7.3	5.0
Capex/revenue (%)	3.1	2.7	0.7	0.4	0.3
Net debt/ (net cash)	13,190.8	15,348.4	17,429.5	16,091.7	13,794.2

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  
leejuy@maybank.com

**Dr Zamros DZULKAFI**  
(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) 6231 8467  
hana.thuluong@maybank.com

### FX

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

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

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

### STRATEGY

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

### FIXED INCOME

**Winson PHOON, CFA**  
Head of Fixed Income  
(65) 6340 1079  
winsonphoon@maybank.com

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

### PORTFOLIO STRATEGY

**CHAN Han Chin**  
(603) 2297 8888  
hanchin.chan@maybank-ib.com

**ONG Seng Yeow**  
(65) 6231 5839  
ongsengyeow@maybank.com

### MIBG SUSTAINABILITY RESEARCH

**Jigar SHAH**  
Head of Sustainability Research  
(91) 22 4223 2632  
jigars@maybank.com

**Neerav DALAL**  
(91) 22 4223 2606  
neerav@maybank.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

### 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  
• Renewable Energy • REITs

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

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

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

**Eugene HOO Yee Hui**  
(603) 2082 6819  
eugene.hoo@maybank.com

**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

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

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

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

**Jarick SEET**  
(65) 6231 5848 jarick.seet@maybank.com  
• Technology

### 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.rodriquez@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 • Gaming

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

### THAILAND

**Malcolm LUI, CFA Head of Research**  
(66) 2658 6300 ext 1399  
malcolm.lui@maybank.com  
• Strategy

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

**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

### INDONESIA

**Jeffrosenberg CHENLIM Head of Research**  
(62) 21 8066 8680  
Jeffrosenberg.lim@maybank.com  
• Strategy • Banking & Finance

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

**Richard SUHERMAN**  
(62) 21 8066 8691  
richard.suherman@maybank.com  
• Metals & Mining

**Etta Rusdiana PUTRA**  
(62) 21 8066 8683  
etta.putra@maybank.com  
• Telcos

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

### VIETNAM

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

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

**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 Discretionary

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

**Nguyen Le Tuan Loi**  
(84 28) 44 555 888 ext 8088  
loi.nguyen@maybank.com  
• Industrials

**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



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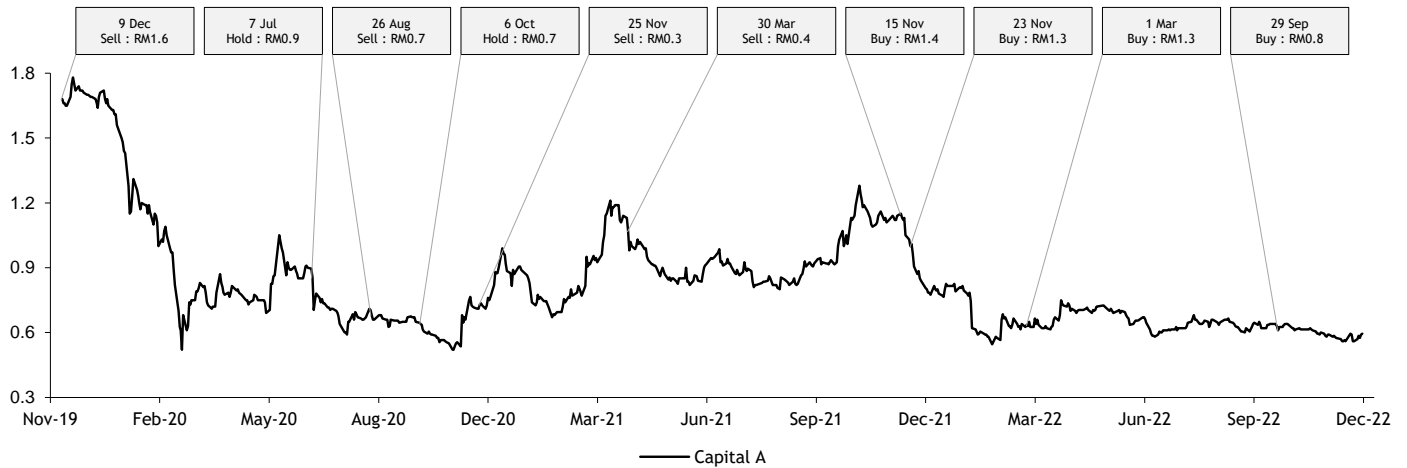
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### Malaysia

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

### 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

### 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)

### 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

### 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

### Vietnam

Maybank Securities Limited  
Floor 10, Pearl 5 Tower,  
5 Le Quy Don Street,  
Vo Thi Sau Ward, District 3  
Ho Chi Minh City, Vietnam

Tel : (84) 28 44 555 888

Fax : (84) 28 38 271 030

### 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

### 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

### 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

#### 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

[www.maybank.com/investment-banking](http://www.maybank.com/investment-banking)  
[www.maybank-keresearch.com](http://www.maybank-keresearch.com)