

Malaysia Software & Tech Services

POSITIVE

[Unchanged]

Digitalisation adoption continues

Maintain POSITIVE; top picks MyEG and CTOS

We maintain our POSITIVE stance on the Malaysia software sector. Share prices of the companies under our coverage have declined by 18-51% YTD, despite industry earnings growing by 12% YoY in 9M22, largely due to the broad market weakness and growing concerns of an economic slowdown. We expect industry earnings to grow by 10% in CY23E, after +15% in CY22E, anchored by the structural shift towards digitalisation and adoption of cashless payments. Our preferred BUYs are MyEG and CTOS, premised on their earnings resilience and strong revenue-recurring business model. We downgrade GHL to HOLD after the recent strong share price appreciation.

Analyst

Shafiq Kadir, CFA
(603) 2297 8691
msshafiqk.abkadir@maybank-ib.com

Strong showing in 9M22 earnings

Industry core net profit grew by 12% YoY in 9M22, largely driven by the economic reopening, which boosted consumer spending, business activities, as well as greater degree of digitalisation through the services offered by the companies under our coverage. For the payment companies, aggregate TPV grew by 14% in the 9M22 period, tracking the total national transaction value for e-payments, which grew by 43% during the same period.

Digitalisation shift to continue

The digitalisation shift should continue to support the industry earnings growth. On the payments side, about 64% of point of sale purchases in Malaysia was still made via cash in 2020, according to FIS, indicating a huge opportunity for the cashless industry to grow. Payment companies could also benefit from the next POS terminal upgrade cycle to meet the ever changing industry security and feature requirements. The proliferation of alternative digital lending providers such as BNPL players could also anchor the growing demand for credit assessment solutions, as provided by CTOS.

Key risks to the industry

There are however signals of moderating economic growth, which may impede both consumer and business spending. This may have a repercussion on the TPV growth of the payment companies, as well as other digital services provided by MyEG and CTOS. Our current industry earnings growth of 10% in CY23E implies a slight moderation from CY22E (+15%), though still growing as the companies may also benefit from new business avenues through the diversification initiatives that they have put in place i.e. MyEG's blockchain business, CTOS' associates cross-selling and cross-expertise opportunities, as well as the payment companies' incorporation of more payment solutions into their terminals.

Abbreviations:

FIS = Fidelity National Information Services Inc
EDC= Electronic data capture
POS = Point of sales
TPV = Transaction processed value
BNPL= Buy now pay later
MDR = Merchant discount rate

Stock	Bloomberg code	Mkt cap (USD'm)	Rating	Price (LC)	TP (LC)	Upside (%)	P/E (x)		P/B (x)		Div yld (%)	
							22E	23E	22E	23E	22E	23E
MyEG	MYEG MK	1,525	Buy	0.89	1.37	55	19.4	18.1	3.8	3.3	1.6	1.7
CTOS Digital Berl	CTOS MK	724	Buy	1.38	1.94	42	36.5	31.1	5.8	5.6	1.4	1.7
GHL Systems	GHLS MK	249	Hold	0.96	0.95	(1)	42.3	35.6	2.2	2.0	2.6	0.0
Revenue Group	REVENUE MK	77	Buy	0.72	1.05	47	33.3	30.0	3.8	2.6	0.0	0.0

1. Strong showing in 9M22 earnings

9M22 sector core earnings up 12% YoY

Industry core net profit grew by 12% YoY in 9M22, largely driven by the economic reopening factor, which boosted consumer spending, business activities, as well as greater degree of digitalisation through the services offered by the companies under our coverage. MyEG made up the bulk of the industry earnings at 77% of the aggregate, followed by CTOS at 17%, and the payment companies at 6%. While both MyEG and CTOS saw positive earnings growth during the period, the payment companies however recorded decline in earnings, owing to margin compression from rising cost of operations despite growing TPV.

Fig 1: Sector core net profit trend

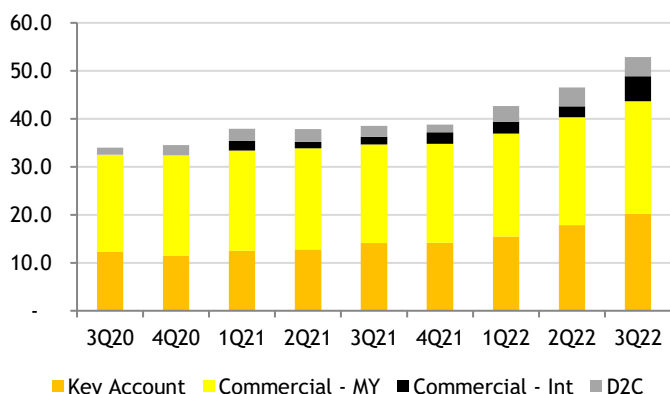
MYRm			Quarterly			Cumulative		
	3Q22	3Q21	% YoY	2Q22	% QoQ	9M22	9M21	% YoY
MyEG	88.8	78.5	13	88.7	0	262.1	235.5	11
CTOS	22.8	13.3	71	22.5	1	57.7	37.0	56
GHL System	7.8	7.4	5	6.2	26	19.0	23.2	(18)
Revenue Group	(2.0)	3.5	nm	0.6	nm	3.2	8.5	(62)
Total core net profit	117.4	102.7	14	118.0	(1)	342.0	304.2	12

Source: Company

MyEG benefited from the stronger performance of its immigration and transport segments, which cushioned the declining healthcare revenue as a result of relaxation of screening and quarantine requirements. MyEG also benefited from the sale of Zetrix tokens, in tandem with the launch of several key applications on its blockchain platform since early 2022. Its 3Q22 core net profit of MYR88.7m was flat QoQ but was up 13% YoY.

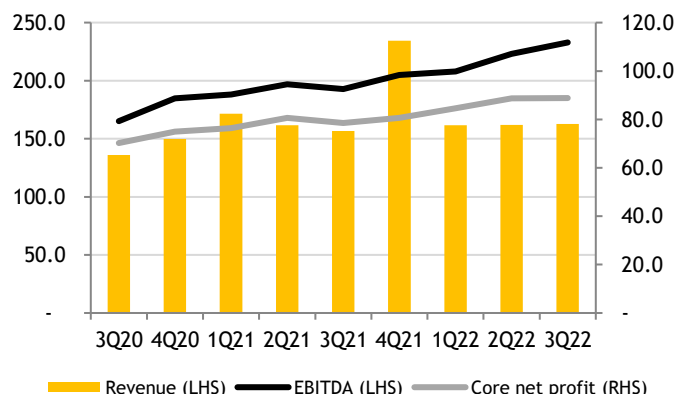
On CTOS, 3Q22 core net profit rose 71% YoY to MYR22.8m. Key Account segment saw higher transactional volumes of its digital reports especially among digital moneylenders, signalling active credit lending activities. CTOS' value-added digital services also saw strong take-up rate across Key Account and Commercial clients. Its retail segment, D2C, also saw a healthy growth in registered users to 2.4mil in 3Q22 (from 2.2mil in 2Q22).

Fig 2: CTOS - Revenue by segment (MYRm)



Source: Company

Fig 3: MyEG's revenue, EBITDA and core NP trend (MYRm)

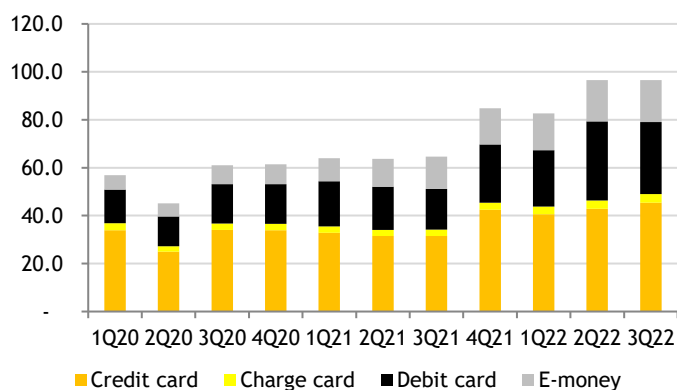


Source: Company

TPV growth helped cushioned the impact of rising costs

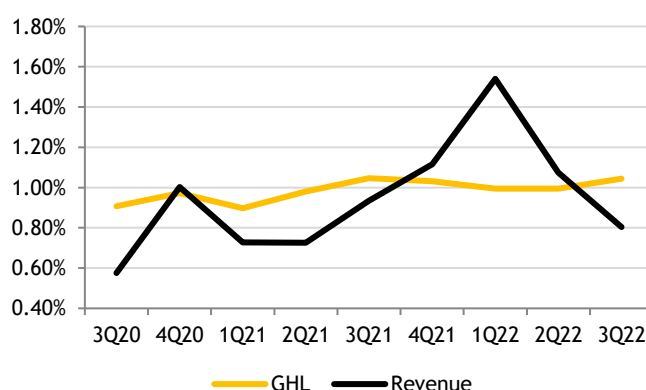
For the payment companies, their aggregate TPV grew by 14% YoY in the 9M22 period, tracking the total national transaction value for e-payments, which grew by 43% during the same period. This was boosted by the strong spending recovery, which continued on its momentum since the economic reopening, festive seasons, as well as a boost from the EPF withdrawals. The blended merchant discount rate (MDR) for the payment companies trended differently, with GHL being more stable, while Revenue had a patchier trend, likely due to volatile merchant mix throughout the period.

Fig 4: Total value of Malaysia’ electronic payment transactions by type (MYRbn)



Source: Bank Negara Malaysia

Fig 5: Blended MDR trend - GHL System vs Revenue Group



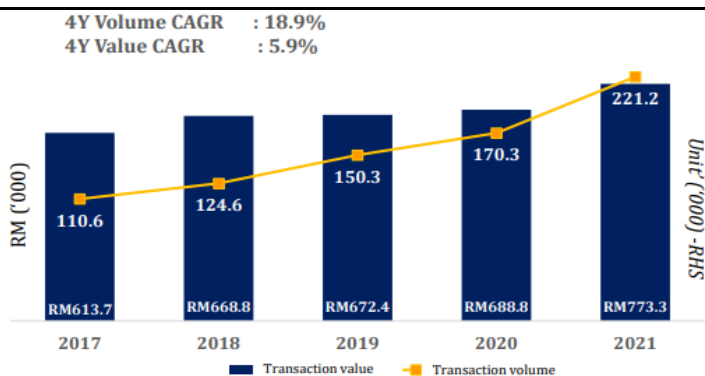
Source: Company

2. Digitalisation shift to continue

Cashless adoption to rise over time

The digitalisation shift should continue to support the industry earnings growth. On the payments side, about 64% of point of sale purchases in Malaysia was still made via cash in 2020, according to FIS, indicating a huge opportunity for the cashless industry to grow. This is supported by the e-payment statistics from Bank Negara Malaysia, where it showed strong transaction value and volume growth, indicating rising adoption of e-payment solutions across the population. Between 2017 and 2021, the total e-payment transaction volume and value per capita grew at a 4-year CAGR of 18.9% and 5.9%, respectively. This trend accelerated throughout the pandemic period, which saw a strong pick up in the growth rates as spending on the digital channels spiked up.

Fig 6: Malaysia’s e-payment transaction per capita



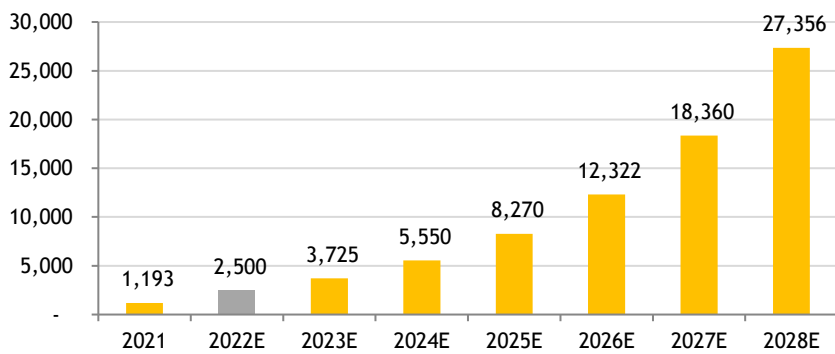
Source: Bank Negara Malaysia

The payment companies have also broadened their payments solutions to be able to accept a greater variety of payment types, schemes and compatibility with various regional e-wallets as part of growing their market reach. On the regulatory front, the central bank also rolled out the national QR code, *DuitNow*, which allows payments from any participating Bank and e-wallets through a single interoperable QR code. The adoption of *DuitNow* is becoming more prevalent among the small merchants and traders due to its low cost and easy to set up.

Proliferation of digital alternative lenders

The proliferation of digital alternative lenders, namely the Buy Now Pay Later (BNPL) players, have also provided an alternative avenue for growth for the software technology companies under our coverage. This has prompted payment companies such as GHL to partner up with the likes of Atome, Split as well as Ablr since 2021 as the popularity of BNPL grows. Deloitte projected that the BNPL payments could grow by 109% in 2022E to reach MYR2.5b, and to expand steadily at a CAGR of 49% between 2022 and 2028 to eventually reach MYR27.4b, signaling the significant growth opportunity within the space. That said, the contribution from these easy payment schemes is still very small in comparison to the overall TPV (<1%) of the payment companies, although we believe this may grow over time as the payment option becomes more prevalent among the consumers.

Fig 7: Malaysia’s BNPL industry payments growth projection (MYRm)



Source: Deloitte & Mambu Guide to BNPL

Moreover, there is also regulatory tailwind from the possible enactment of Consumer Credit Act by BNM on BNPL providers as part of BNM regulating the booming digital alternative lending industry. This could also be an additional catalyst for the likes of CTOS as they could offer greater variety of their digital credit assessment and lending solutions to the BNPL players.

3. Earnings outlook

Projecting earnings growth of 9.8% in CY23E

We project the industry earnings to grow by 9.8% in FY23E, following a growth of 15.2% in FY22E. This implies a slowdown in the growth rate, which could be explained by CTOS' strong expected core net profit growth in FY22E due to the tax writebacks and renewal of its pioneer tax status. We still project a steady earnings growth rate across the software tech companies under our coverage.

Fig 8: Sector core net profit trend

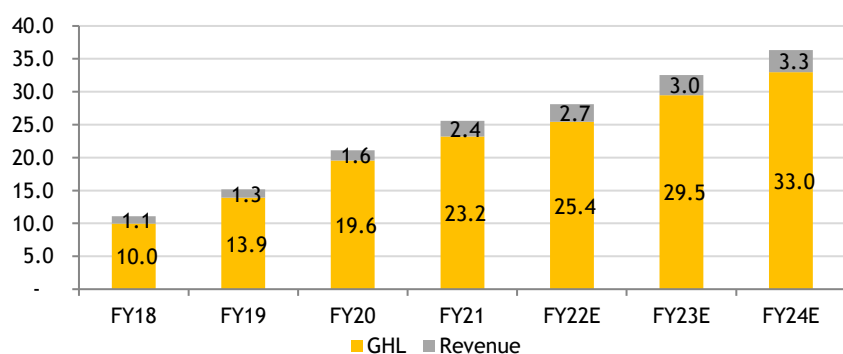
MYRm	CY19	CY20	CY21	CY22E	CY23E	CY24E
MyEG	303.1	267.1	316.1	346.1	370.4	416.5
CTOS	39.5	42.8	49.6	87.2	102.5	119.3
GHL System	28.7	30.7	31.4	25.9	30.8	36.4
Revenue Group	8.1	9.5	12.3	12.3	14.1	19.2
Total core net profit	379.4	350.1	409.4	471.5	517.9	591.3
% growth		-7.7%	17.0%	15.2%	9.8%	14.2%

Source: Company, Maybank IBG Research

Payments - Industry TPV, EDC terminal upgrade cycle

We project the aggregate TPV of both GHL and Revenue to grow by 16% in FY23E, following an expected +10% in FY22E, and +21% in FY21. This could be driven by the growing number of merchants and touchpoints through direct acquiring initiatives, as well as the ongoing shift towards cashless payments by the population. For GHL, we expect a much stronger TPV growth of 15% in FY23E vs Revenue's 12%, premised on the upcoming direct acquiring licenses that will be granted to the group in Thailand and Philippines. This could enable GHL to directly acquire smaller sized merchants, thus boosting its total touchpoints across the region.

Fig 9: Industry TPV growth projection for GHL and Revenue (MYRb)



Source: Company, Maybank IBG Research

Business diversification to other digital-based solutions

Some companies have also pursued new business avenues through their diversification initiatives to generate new growth opportunities. MyEG's blockchain business has been progressing relatively well, with various key applications introduced onto the platform such as smart contracts and cross-border supply chain financing, both of which could see sizeable market adoption, in our view. Elsewhere, CTOS could also leverage on its associates i.e. BOL, JurisTech and RAM Holdings for cross-selling and cross-expertise opportunities, which could further strengthen its market-leading position in providing innovative credit lending solutions.

4. Valuations

We have BUYs on MyEG and CTOS, premised on their stable recurring business model, strong business moat and ongoing business diversification efforts into offering value-added services. On the payments side, we downgrade GHL to HOLD after the recent strong share price appreciation. We maintain a BUY on Revenue as the recent share price weakness may have adequately reflected near term challenges from potential softening of consumer spending. Its continuous investments to meet the ever growing stringent security and feature requirements could also translate to growth for both GMV and terminal maintenance income.

In general, valuations have become more palatable, with PERs moderating to between -1SD and average of the 3-year historical averages for the software companies under our coverage (ex GHL).

Fig 10: Peer comparison table

Company	Mkt cap (MYRm)	Rec	Price (MYR)	TP (MYR)	PE (x)		EV/EBITDA (x)		Yield (%)	
					FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
MyEG	6,718	BUY	0.89	1.37	19.4	18.1	16.4	15.2	1.6	1.7
CTOS	3,188	BUY	1.38	1.94	36.5	31.1	40.2	31.3	1.4	1.7
GHL System	1,096	HOLD	0.96	0.95	42.3	35.6	14.2	12.2	2.6	0.0
Revenue Group	333	BUY	0.72	1.05	33.0	30.0	9.1	7.0	0.0	0.0
Simple average					33.0	28.7	20.0	16.4	1.5	0.9

Source: Bloomberg (share prices as at 9 Dec 2022 close), Maybank IBG Research

5. Key risks

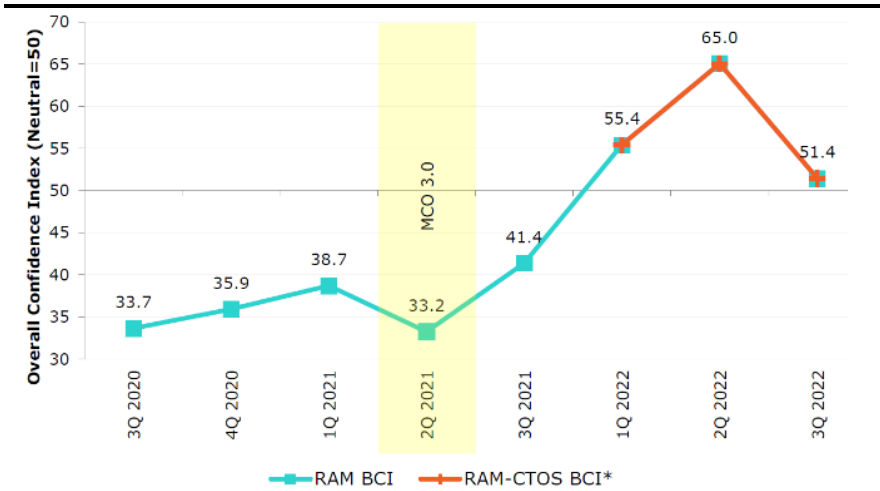
Softening consumer spending

Consumer spending power in 2023 could be negatively impacted by ongoing rising interest rates, potential removal of blanket subsidies and the general inflationary environment, all of which can reduce discretionary spending and eventually the TPV growth of the payments companies. Following a 100 basis point hike on the overnight policy rate (OPR) in 2022, our in-house economic team is projecting another 25 basis point hike in 2023. Additionally, the new Government could be looking to rationalise the subsidy allocation, which may translate to rising prices of certain essential items such as petrol.

Business confidence index have moderated

The latest RAM-CTOS Business Confidence Index also showed sequential weakness, where the index fell from 65.0 in 2Q22 to 51.4 in 3Q22. While still above the neutral benchmark of 50.0, firms involved in the survey generally cited rising cost of doing business as the main concern as the inflationary impact lasted longer than expected. Elsewhere, businesses also cited labour constraints as another big challenge that is affecting business operations. These factors could negate the positive effects coming from the economic reopening, in our view.

Fig 11: RAM-CTOS BCI - Waning sentiments among businesses in 3Q 2022



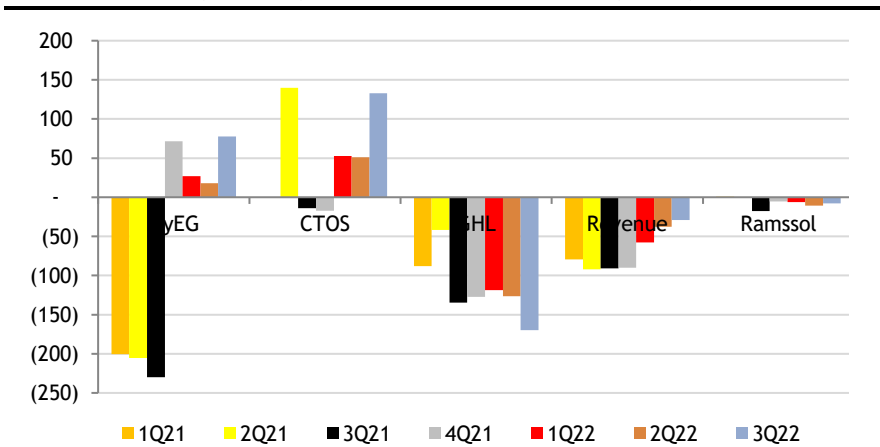
Source: RAM Holdings Bhd

Ongoing high capital expenditure on new expansion initiatives

The year of 2022 has seen both MyEG and CTOS swung from net cash to a net debt balance sheet position, owing to their elevated investment cycle to fund the development of new business avenues, or acquisition of value-accretive entities that could complement their existing businesses. Revenue’s net cash position has also narrowed over the period due to the acquisition on two properties in Kuala Lumpur in 4Q21, totaling MYR44m.

Across the companies under our coverage, the risk of an elevated capex cycle is most prevalent for MyEG in our view, as the management has previously hinted on continuous spending on the development of its Zetrix blockchain platform to cater for a greater variety of applications. CTOS, on the other hand, has signaled that they are ceasing their stake acquisition spree on its associates, namely BOL Thailand, JurisTech and RAM Holdings, citing current position as ample for them to execute the necessary business strategies and extract the synergies with its associate companies. This may provide a cap on its net gearing, which stood at 26% as at 3Q22. As for both GHL and Revenue, we expect a stable capex run-rate for both companies.

Fig 12: Net debt/(net cash) position of the companies (MYRm)



Source: Company

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 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) 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

Florenzo de JESUS
(63) 2 8849 8846
florenzo.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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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, 22nd 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,
 20th - 21st Floor,
 Rama 1 Road Pathumwan,
 Bangkok 10330, Thailand

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

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

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, 11th 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

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