

Lotte Chemical Titan (TTNP MK)

3Q23 results preview: Not out of the woods yet

Revise FY23-25E forecasts; Maintain SELL

We revise FY23-25E earnings forecast to -MYR1.0b/-MYR701m/+MYR176m respectively (from -MYR833m/-MYR104m/+MYR154m previously) to reflect higher average naphtha feedstock price assumptions of USD680/USD640/USD600/tonne in FY23-25E. Following the downward revision in our earnings estimates, we reiterate SELL with a reduced TP of MYR0.84 (from MYR1.01 previously), based on a FY24E P/BV multiple of 0.15x, the latter reflecting trough historical P/BV trading range multiple (Fig 1) as we expect the group to book record losses this year.

3Q23 should register narrower losses QoQ...

LCTITAN's 3Q23 results are tentatively scheduled for release on 26 Oct 2023 and we expect core loss for the quarter to range between -MYR150m-200m, barring any unforeseen swings in cost/expenses. Based on our findings, we estimate polymer prices to be lower QoQ by -3% to -5% in 3Q23 but input naphtha prices (booking in a 6-week lag) were down substantially by -17% throughout the quarter. This essentially means that the group should register significant cost reductions despite expectations of lower ASPs in 3Q23. Our 3Q23 core loss estimate indicates that 9M23's cumulative losses would range from -MYR651m to -MYR701m, making up about 65-70% of our revised FY23E full-year forecast.

...but losses are expected to expand again in 4Q23

As at the point of writing, accounting for a 6-week lag, naphtha prices (based on the Naphtha Japan Index) have risen 14% from mid-July till mid-Oct 2023. On the flipside, polymer prices have been relatively flat which effectively caps the upside to ASPs throughout the quarter. With the expectations of heightened costs coupled with weak ASPs in 4Q23, we think that LCTITAN's net losses will expand again in 4Q23, underscoring the fact that the group is not yet out of the woods, in our view.

High oil price environment a bane to LCTITAN

Based on our in-house Brent Crude Oil price ASP forecast of USD85-80 for 2023-2024E, we think that the operating environment will still be tough for LCTITAN as input naphtha prices will continue to remain elevated. With that, we view that LCTITAN will still be loss-making in FY24E. Maintain SELL.

FYE Dec (MYR m)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	9,831	10,019	7,560	8,497	9,291
EBITDA	1,647	(457)	(779)	(185)	1,077
Core net profit	991	(616)	(1,004)	(701)	176
Core EPS (sen)	43.5	(27.0)	(44.1)	(30.8)	7.7
Core EPS growth (%)	446.9	nm	nm	nm	nm
Net DPS (sen)	38.9	14.0	0.0	0.0	3.9
Core P/E (x)	5.0	nm	nm	nm	14.9
P/BV (x)	0.4	0.3	0.2	0.3	0.3
Net dividend yield (%)	17.8	9.8	0.0	0.0	3.4
ROAE (%)	8.5	(6.0)	(8.9)	(6.7)	1.7
ROAA (%)	6.7	(3.8)	(5.5)	(3.2)	0.7
EV/EBITDA (x)	2.3	nm	nm	nm	15.8
Net gearing (%) (incl perps)	net cash	net cash	21.2	64.0	90.9
Consensus net profit	-	-	(833)	(36)	226
MIBG vs. Consensus (%)	-	-	(20.6)	(1,876.0)	(22.3)

Jeremie Yap

jeremie.yap@maybank-ib.com

(603) 2297 8688

SELL

Share Price	MYR 1.15
12m Price Target	MYR 0.84 (-27%)
Previous Price Target	MYR 1.01

Company Description

Lotte Chemical Titan manufactures and sells petrochemicals and polymers

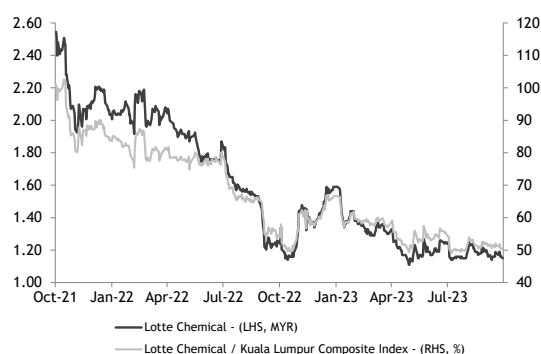
Statistics

52w high/low (MYR)	1.59/1.11
3m avg turnover (USDm)	0.2
Free float (%)	21.5
Issued shares (m)	2,312
Market capitalisation	MYR2.7B USD558M

Major shareholders:

Lotte Chemical Corp.	74.7%
Permodalan Nasional Bhd.	2.6%
Lotte Chemical Titan Holding Bhd.	1.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(5)	(8)	(9)
Relative to index (%)	(4)	(10)	(8)

Source: FactSet

ESG@MAYBANK IBG

jeremie.yap@maybank-ib.com

Risk Rating & Score ¹	26.3 (Medium)
Score Momentum ²	-0.4
Last Updated	20 Apr 2023
Controversy Score ³ (Updated: NA)	NA

Business Model & Industry Issues

- As an integrated chemicals producer, LCT’s biggest ESG challenge lies in the negative sentiment surrounding single-use plastics. We estimate that the single-use plastics account for c. 10% of its total capacity. That said, LCT is looking to develop biodegradable polymers and energy saving products. Additionally, LCT can tap onto its parent Lotte Chemical Corporation’s (011170 KS, CP: KRW130,200, Not rated) technologies for more eco-friendly products.
- Its corporate governance appears robust, with a majority of the Board composed of Independent Directors, though there was a lack of guidance on the impact of the water supply cut back in 2017, during its IPO roadshow.
- We are positive on the sector’s long-term growth as we believe global demand for plastics will remain robust given there are no real alternatives, while the industry will continuously improve on environment-friendly processes and product innovations. On the flip side, we think that the current environment (where crude oil prices are expected to remain elevated in the medium term) is extremely harsh for naphtha-based petrochemical businesses.

Material E issues

- In FY22, LCTITAN’s Malaysia operations air emissions data are as follows: (NO_x: 510.3t; SO_x: 5.5t; CO: 174.0t; Particulate Matter: 28.4t). FY21 data: (NO_x: 695.2t; SO_x: 8.2t; CO: 210.7t; Particulate Matter: 40.0t). All air emission matrices declined YoY.
- In FY22, Malaysia operations energy intensity: 0.330ktoe/kT (FY21: 0.326ktoe/kT).
- In FY22, Malaysia operations water consumption intensity: 5,060m³/kT (FY21: 5,063m³/kT).
- In FY22, Malaysia operations hazardous waste generation: 700.3t (FY21: 608.6t). FY22 total recycled waste: 900.4t (FY21: 861.6t).
- Zero compounds and court cases arising from environmental compliance in Malaysia.

Material S issues

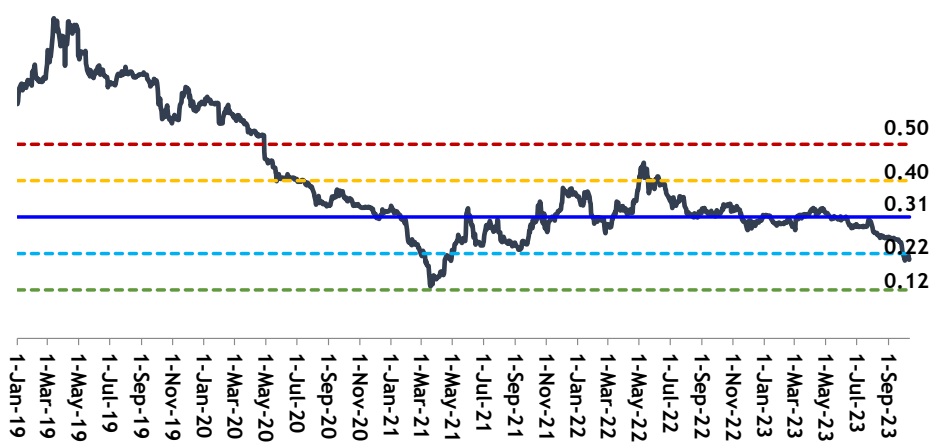
- In FY22, LCTITAN achieved zero fatalities in Malaysia and Indonesia operations.
- FY22 Lost Time Accidents: 3 (FY21: 3).
- FY22 Malaysia operations Customer Satisfaction Rate: 100% (FY21: 100%).
- Continued collaboration with schools on Rainwater Harvesting Project.
- FY22 total training hours: 33.7k hours (FY21: 30.6k hours). FY22 average training hours per employee: 29.1k hours (FY21: 28.7k hours).
- FY22 male:female employee ratio (82:18) - similar to FY21.
- 22% of LCTITAN’s Malaysian operations workforce is below the age of 30, 63% between the age of 30-50, 15% above the age of 50.
- LCTITAN do not offer part-time employment. All employees are employed on a full-time basis.

Key G metrics and issues

- LCTITAN’s Board comprises 7 Directors - 4 Independent Non-Executive Directors, 1 Non-Independent Non-Executive Director, 2 Non-Independent Executive Directors.
- A relatively experienced and gender-diversified board - 86% are above 50 years old and 43% are female.
- Independent directors form 100% / 75% / 67% of audit / risk / nomination & remuneration committee.
- 5 of its Board members are Malaysians, the remaining 2 are Koreans.
- Has set a dividend payout policy of 50% of net profit.
- Has a Whistleblowing Policy and Anti-Bribery & Anti-Corruption Manual.
- Audited by KPMG (one of the Big Four Accounting Firms).
- Since FY18, LCTITAN has adopted integrated reporting, in accordance with the principles prescribed by the International Integrated Reporting Council Framework.
- In Aug 17, LCTITAN’s share price plunged as the shareholders were caught off guard by the poor 2Q17 results that were mainly caused by an unplanned water supply disruption at its plant in Johor. Though LCT disclosed the water supply disruption in its IPO prospectus, the significance of the impact was not made clear.

¹**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. ²**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. ³**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: Historical 1-year forward P/BV band



Source: Maybank IBG Research

Risk statement

There are several risk factors that may impact our earnings estimates, target price and SELL rating for LCTITAN. Key upside risks include: (i) a faster-than-expected recovery in polymer/monomer prices; and (ii) a sudden decline in crude oil/naphtha prices.

FYE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Key Metrics					
P/E (reported) (x)	5.3	nm	nm	nm	14.9
Core P/E (x)	5.0	nm	nm	nm	14.9
P/BV (x)	0.4	0.3	0.2	0.3	0.3
P/NTA (x)	0.4	0.3	0.2	0.3	0.3
Net dividend yield (%)	17.8	9.8	0.0	0.0	3.4
FCF yield (%)	14.4	nm	nm	nm	nm
EV/EBITDA (x)	2.3	nm	nm	nm	15.8
EV/EBIT (x)	3.5	nm	nm	nm	30.6

INCOME STATEMENT (MYR m)

Revenue	9,830.9	10,019.1	7,560.2	8,497.3	9,291.4
EBITDA	1,647.4	(457.1)	(778.7)	(184.8)	1,076.5
Depreciation	(556.4)	(584.3)	(520.0)	(520.0)	(520.0)
Amortisation	0.0	0.0	0.0	0.0	0.0
EBIT	1,091.0	(1,041.5)	(1,298.7)	(704.8)	556.5
Net interest income / (exp)	38.7	32.3	(14.3)	(245.5)	(350.9)
Associates & JV	203.1	7.6	(50.0)	20.0	20.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	1,332.8	(1,001.5)	(1,363.0)	(930.3)	225.7
Income tax	(292.0)	256.5	327.1	223.3	(54.2)
Minorities	(0.8)	14.0	31.9	5.6	4.1
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Reported net profit	1,040.0	(731.1)	(1,004.0)	(701.5)	175.6
Core net profit	990.9	(615.7)	(1,004.0)	(701.5)	175.6

BALANCE SHEET (MYR m)

Cash & Short Term Investments	1,842.0	1,305.0	1,737.5	1,016.7	2,104.1
Accounts receivable	975.3	919.6	693.9	779.9	852.8
Inventory	1,674.3	1,461.9	1,103.1	1,239.9	1,355.7
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	5,254.3	9,598.8	13,078.8	17,558.8	21,038.8
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	2,362.9	2,514.1	2,464.1	2,484.1	2,504.1
Other assets	3,366.0	972.4	972.4	972.4	972.4
Total assets	15,474.8	16,771.8	20,049.8	24,051.8	28,827.9
ST interest bearing debt	0.0	0.0	1,000.0	2,000.0	3,000.0
Accounts payable	974.7	1,166.0	879.8	988.9	1,081.3
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	0.0	0.0	3,600.0	7,200.0	10,800.0
Other liabilities	1,172.0	1,082.0	1,082.0	1,082.0	1,082.0
Total Liabilities	2,146.6	2,248.2	6,562.0	11,271.1	15,963.5
Shareholders Equity	12,705.6	11,757.9	10,753.9	10,052.4	10,140.2
Minority Interest	622.6	2,765.7	2,733.9	2,728.3	2,724.2
Total shareholder equity	13,328.2	14,523.6	13,487.8	12,780.7	12,864.5
Total liabilities and equity	15,474.8	16,771.8	20,049.8	24,051.8	28,827.9

CASH FLOW (MYR m)

Pretax profit	1,332.8	(1,001.5)	(1,363.0)	(930.3)	225.7
Depreciation & amortisation	556.4	584.3	520.0	520.0	520.0
Adj net interest (income)/exp	(38.7)	(32.3)	0.0	0.0	0.0
Change in working capital	(441.7)	12.4	298.3	(113.7)	(96.3)
Cash taxes paid	(65.7)	(102.3)	327.1	223.3	(54.2)
Other operating cash flow	(166.2)	197.5	50.0	(20.0)	(20.0)
Cash flow from operations	1,167.7	(348.9)	(167.5)	(320.8)	575.2
Capex	(449.1)	(4,337.6)	(4,000.0)	(5,000.0)	(4,000.0)
Free cash flow	718.6	(4,686.5)	(4,167.5)	(5,320.8)	(3,424.8)
Dividends paid	(474.0)	(796.7)	0.0	0.0	(87.8)
Equity raised / (purchased)	135.4	2,142.4	0.0	0.0	0.0
Change in Debt	0.0	0.0	4,600.0	4,600.0	4,600.0
Other invest/financing cash flow	166.8	2,749.4	0.0	0.0	0.0
Effect of exch rate changes	26.9	54.5	0.0	0.0	0.0
Net cash flow	573.7	(537.0)	432.5	(720.8)	1,087.4

FYE 31 Dec	FY21A	FY22A	FY23E	FY24E	FY25E
Key Ratios					
Growth ratios (%)					
Revenue growth	42.4	1.9	(24.5)	12.4	9.3
EBITDA growth	98.4	nm	nm	nm	nm
EBIT growth	301.0	nm	nm	nm	nm
Pretax growth	553.4	nm	nm	nm	nm
Reported net profit growth	599.9	nm	nm	nm	nm
Core net profit growth	448.0	nm	nm	nm	nm
Profitability ratios (%)					
EBITDA margin	16.8	nm	nm	nm	11.6
EBIT margin	11.1	nm	nm	nm	6.0
Pretax profit margin	13.6	nm	nm	nm	2.4
Payout ratio	85.2	nm	0.0	0.0	50.0
DuPont analysis					
Net profit margin (%)	10.6	nm	nm	nm	1.9
Revenue/Assets (x)	0.6	0.6	0.4	0.4	0.3
Assets/Equity (x)	1.2	1.4	1.9	2.4	2.8
ROAE (%)	8.5	(6.0)	(8.9)	(6.7)	1.7
ROAA (%)	6.7	(3.8)	(5.5)	(3.2)	0.7
Liquidity & Efficiency					
Cash conversion cycle	56.3	50.6	49.3	40.8	42.9
Days receivable outstanding	31.3	34.0	38.4	31.2	31.6
Days inventory outstanding	62.6	52.2	54.0	47.4	55.5
Days payables outstanding	37.5	35.6	43.0	37.8	44.3
Dividend cover (x)	1.2	(2.3)	nm	nm	2.0
Current ratio (x)	7.4	2.4	2.5	2.1	3.2
Leverage & Expense Analysis					
Asset/Liability (x)	7.2	7.5	3.1	2.1	1.8
Net gearing (%) (incl perps)	net cash	net cash	21.2	64.0	90.9
Net gearing (%) (excl. perps)	net cash	net cash	21.2	64.0	90.9
Net interest cover (x)	na	32.3	na	na	1.6
Debt/EBITDA (x)	0.0	0.0	nm	nm	12.8
Capex/revenue (%)	4.6	43.3	52.9	58.8	43.1
Net debt/ (net cash)	(1,842.0)	(1,305.0)	2,862.5	8,183.3	11,695.9

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

Dr Zamros DZULKAFI
Malaysia | Philippines
(603) 2082 6818
zamros.d@maybank-ib.com

Erica TAY
China | Thailand
(65) 6231 5844
erica.tay@maybank.com

Brian LEE Shun Rong
Indonesia | Singapore | Vietnam
(65) 6231 5846
brian.lee1@maybank.com

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

Luong Thu Huong
(65) 6231 8467
hana.thuhuon@maybank.com

FX

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

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

Alan LAU
(65) 6320 1378
alanlau@maybank.com

Shaun LIM
(65) 6320 1371
shaunlim@maybank.com

STRATEGY

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

FIXED INCOME

Winson PHOON, FCA
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

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
• Equity Strategy
• Non-Bank Financials (stock exchange)
• Construction & Infrastructure

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

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

LOH Yan Jin
(603) 2297 8687
lohyanjin.loh@maybank-ib.com
• Ports • Automotive • Technology (EMS)

Jeremie YAP
(603) 2297 8688
jeremie.yap@maybank-ib.com
• Oil & Gas • Petrochemicals

Arvind JAYARATNAM
(603) 2297 8692
arvind.jayaratnam@maybank.com
• Technology (Semicon & Software)

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 5849
ericong@maybank.com
• Healthcare • Transport • SMIDs

Kelvin TAN
(65) 6231 5837
kelvin.tan1@maybank.com
• Telcos • Industrials

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

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

Krishna GUHA
(65) 6231 5842
krishna.guha@maybank.com
• REITs

PHILIPPINES

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

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

Alexa Mae CARVAJAL
(63) 2 8849 8838
alexamae.carvajal@maybank.com
• Consumer • Gaming • Property • REITs

THAILAND

Chak REUNGSINPINYA *Head of Research*
(66) 2658 5000 ext 1399
chak.reungsinpinya@maybank.com
• Strategy • Energy

Jesada TECHAHUSDIN, CFA
(66) 2658 5000 ext 1395
jesada.t@maybank.com
• Banking & Finance

Wasu MATTANAPOTCHANART
(66) 2658 5000 ext 1392
wasu.m@maybank.com
• Telcos • Technology • REITs • Property
• Consumer Discretionary

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

Natchaphon RODJANAROWAN
(66) 2658 5000 ext 1393
natchaphon.rodjanarowan@maybank.com
• Utilities

INDONESIA

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

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

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

William Jefferson W
(62) 21 8066 8563
william.jefferson@maybank.com
• Property

Adi WICAKSONO
(62) 21 8066 8686
adi.wicaksono@maybank.com
• Plantations

Satriawan HARYONO, CEWA, 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 8182
loi.nguyen@maybank.com
• Property

Nguyen Thanh Hai
(84 28) 44 555 888 ext 8081
thanhhai.nguyen@maybank.com
• Industrials

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

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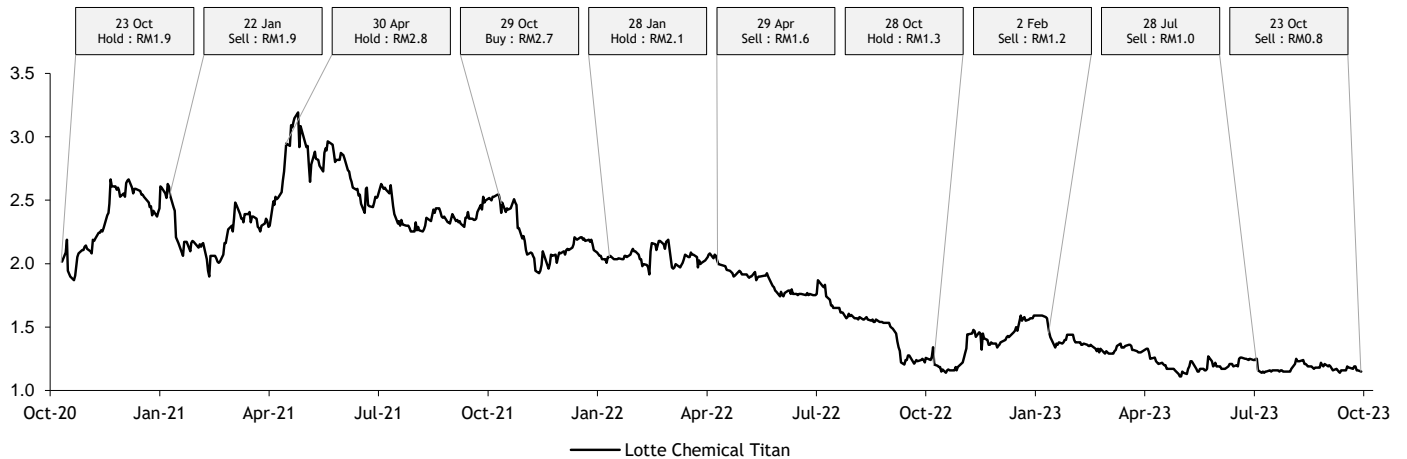
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Malaysia

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, 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)

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

Sales Trading

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.com
Tel: (44) 207-332-0221

India

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

www.maybank.com/investment-banking
www.maybank-keresearch.com