Suntec REIT (SUN SP)

Evaluating risks amid potential

Fundamentals improving; 9M24 DPU in line

SUN's 9M24 DPU fell 12% YoY to SGD4.622cts, in line with the MIBG estimate. DPU from operations was SGD1.58cts (-0.9% YoY), excluding capital top-ups from the divestment of Park Mall. We see signs of SUN's UK assets bottoming out and occupancy of its Australian portfolio improving. Management is cautious about potential valuation dip of SGD200m due to cap rates in the Australian market. We raise our DDM-based TP from SGD1.10 to SGD1.25 after applying a lower risk-free rate of 2.75% (vs from 3.0% previously). Maintain HOLD.

Cautious optimism for Singapore portfolio

Strong rental reversions of Suntec offices (+12.9%) and Suntec City mall (+21.2%) in 3Q24 underpinned management's cautious optimism. Positive rent growth of mid-to-high single digit for Suntec offices is expected to extend into FY25. Management observed for demand for office space of about 5,000 sq ft. Strong shopper traffic (+9% YoY in 3Q24) and stable tenant sales (-1% YoY) account for strong leasing demand (YTD reversion: 20.9%). Meanwhile, occupancy cost crept up to c.23% in 3Q24. Backfilling of Pure Fitness space lifts occupancy at Suntec City Mall by 2.8ppt. Management expects rental reversion of 10-15% in FY25, and stronger topline contribution from the retail portion. Occupancy of its Australia portfolio rose 1.5ppt QoQ, driven by Southgate and 55 Currie Street. Management expects occupancy at 55 Currie Street to further increase by about 5ppt. Backfilling at UK's Minister Building is expected to complete by end-FY24 and contributions should begin in FY25 after the incentive periods. In addition, all lease break terms for assets in its UK portfolio have been removed.

Potential increase in gearing

The cap rate for its Australian portfolio is likely to expand by 50-100bps, which would translate to around SGD200m reduction in valuation. As such, current gearing of 42.3% is expected to tick up to c.43% by year-end, assuming all other valuations remain unchanged. Adjusted ICR is 1.9x, hovering above bank covenant of 1.75x. COD is 4bps higher at 4.06% in Sep'24, as hedges expire. With more forex swaps rolling off in FY25, management estimates COD of 4.2-4.3%.

Other catalysts

Management is planning an AEI for 60,000 sq ft of retail space at Suntec City mall, commencing in 2H25. Management expects an ROI of about 30-40%. Pre-booking status shows less MICE events at the Suntec convention centre in 2025. Nonetheless, SUN expects the top line for the convention centre to hold up, complemented by other corporate and entertainment events. SUN has divested SGD50m of strata office units YTD; its soft target of SGD100M for FY24 is unchanged.

FYE Dec (SGD m)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue	427	463	467	482	487
Net property income	316	313	320	325	329
Core net profit	265	117	185	198	207
Core EPU (cts)	9.3	4.1	6.4	6.7	7.0
Core EPU growth (%)	50.9	(56.2)	57.0	5.8	3.3
DPU (cts)	8.9	7.1	6.9	7.5	7.7
DPU growth (%)	2.4	(19.7)	(2.7)	7.5	2.7
P/NTA (x)	0.6	0.6	0.6	0.6	0.6
DPU yield (%)	6.4	5.8	5.6	6.1	6.2
ROAA (%)	2.3	1.0	1.7	1.8	1.9
Debt/Assets (x)	0.41	0.38	0.38	0.38	0.38
Consensus DPU	-	-	6.1	6.7	7.1
MIBG vs. Consensus (%)	-	-	13.0	11.4	8.0

Li Jialin jialin.li@maybank.com (65) 6231 5845



HOLD

Share Price	SGD 1.23
12m Price Target	SGD 1.25 (+7%)
Previous Price Target	SGD 1.10

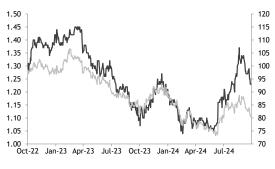
Company Description

SUN is a real estate investment trust that invests in income-producing properties used primarily for office and retail.

Statistics

52w high/low (SGD)	1.37/1.04
3m avg turnover (USDm)	10.3
Free float (%)	73.0
Issued shares (m)	2,909
Market capitalisation	SGD3.6B
	USD2.7B
Major shareholders:	
TANG GORDON	9.1%
CHEN HUAI DAN	7.6%
YANG CHAN ZHEN	6.8%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(8)	4	13
Relative to index (%)	(9)	(1)	(4)
Source: FactSet			

Abbreviations explained

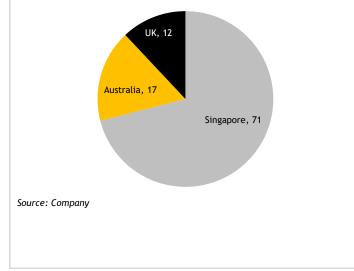
AEI - asset-enhancement initiative COD - Cost of debt ROI - return on investment ICR - interest coverage ratio MICE - meetings, incentives, conferences, and exhibitions



Value Proposition

- Owns a portfolio of office and retail properties in Singapore and Australia valued at SGD12.1b, with its most prominent asset being Suntec City, comprising four office towers, a mall and a convention centre.
- Sponsor ESR has SGD140b of AUM across 14 REITs, private funds and logistics assets, and it's the largest REIT manager in APAC with USD45b in total AUM.
- Gearing at c.43% is high relative to peers, with acquisitions likely to be timed with divestments and/or a placement, given strong share price appreciation.

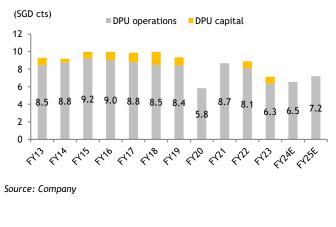
Income contribution by geography



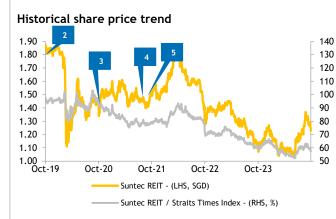
Financial Metrics

- DPUs rebounding from FY21 with the completions and contributions from acquisitions and reopening.
- Suntec City mall occupancy to trend towards 95%, with +15% rent reversion for the retail business in FY24.
- Office vacancies may rise and rent reversion moderate on back of tech rightsizing and ample shadow space.
- DPU may be impacted by higher borrowing cost and lease renewals in overseas offices.

Projected and past DPU



Price Drivers



Source: Company, Maybank IBG Research

- 1. Apr-19: Raises SGD200m in gross proceeds from private placement for potential Australian acquisition.
- 2. Jul-19: Acquires two Australian properties 21 Harris in Sydney for AUD297m at 5.5% NPI yield, and 55 Currie in Adelaide for AUD148.3m at 8.0% NPI yield.
- Oct-20: Acquires first London property a 50% interest in Nova development for GBP430.6m at 4.6% NPI yield at a +4.6% DPU accretion (fully debt-funded).
- 4. Jun-21: Divests 9 Penang Road for SGD295.5m achieving 305% ROI.
- 5. Jun-21: Divests Suntec office strata units at 3.1% yield and acquires Minster Building in London for GBP353.0m at 4.5% yield.

Swing Factors

Upside

- Earlier-than-expected pick-up in leasing demand for office or retail space driving improvement in occupancy.
- Better-than-anticipated rental reversions.
- Accretive acquisitions or redevelopment projects.

Downside

- Prolonged slowdown in economic activity could reduce demand for office and retail space, resulting in lower occupancy and rental rates.
- Termination of long-term leases contributing to weaker portfolio tenant retention rate.
- Sharper-than-expected rise in interest rates could increase cost of debt and negatively impact earnings, with higher Scost of capital lowering valuations.

ESG@MAYBANK IBG

jialin.li@maybank.com

Risk Rating & Score ¹	13 (Low)
Score Momentum ²	+1.0
Last Updated	02 Dec 2022
Controversy Score ³	0
(Updated: 02 Dec 2022)	

Business Model & Industry Issues

- SUN draws on its available pool of funds to invest in commercial real estate, undertake asset enhancements, and redevelop
 properties to optimise value for its unit holders. It is susceptible to sustainability-focused investors with strong preference for
 investing in companies that meet specific ESG criteria, given its incessant need for additional capital.
- Its activities relating to permissible investments, leverage limits and annual reporting requirements are closely regulated by the MAS under Singapore's code on collective investment schemes. Independence, real estate and capital markets experience on its board is high, with strong representation by members with international experience, essential in our view, as its overseas portfolio is increasingly a growth platform.
- Has made efforts to improve the scope of reporting and formalisation of targets since its inaugural sustainability report in FY17, including engaging an independent external consultant in FY19 to help determine and finalise material ESG matters presented to and then approved by the board.
- Achieved the Global Real Estate Sustainability Benchmark's highest 5-star rating in its inaugural participation in FY20.

Material E issues

- Four Singapore properties maintained their BCA Green Mark certifications in FY21; Suntec City Mall and Suntec Singapore both rated Gold, and ORQ and MBFC Platinum. Its Australian assets improved/maintained their environmental and energy ratings certifications.
- In FY21 adopted the market-based approach to account for Scope 2 emissions, to better articulate the impact of renewable energy consumption on its carbon emissions.
- The use of carbon credits to offset emissions due to energy consumption at the common areas was implemented at 177 Pacific Highway and 477 Collins in FY21.
- Maintained an explicit 2024 target to reduce energy intensity by 3.0% and to maintain water intensity, both from a 2019 baseline.
- Secured maiden AUD450m green loan facility in FY20 to finance or refinance eligible assets based on a green finance framework.

Material S issues

- Achieved average training per employee of 32 hours in FY21 (vs 55/35/36 hours in FY18/FY19/FY20), and ahead of its target of 26 hours, despite unavailability of large-scale inperson trainings during the pandemic.
- Gender diversity is high, with female representation at 70% for all employees in FY21 (vs 74%/65% in FY19/FY20), 60% at the management level (in FY19-21), and the Chairman's seat on the board.
- Set up end-of-trip facilities at 177 Pacific Highway to provide amenities for cyclists travelling to work.
- Suntec City has (since FY16) supported The Purple Parade, Singapore's largest movement for inclusion and people with disabilities

Key G metrics and issues

- Externally managed by subsidiaries of ARA, since late 2021
 a part of the ESR group, which supports its growth via a
 pipeline of property assets from its development activities,
 and access to capital markets.
- Board independence is fairly high 4 of its 8 members are independent.
- Management fee structure, with the base fee at <=0.3% of its deposited property, performance fee at 4.5% pa of NPI, as well as acquisition and disposal fee at 1.0% and 0.5% deal value, is comparable to peers.
- Does not disclose the cumulative remuneration of its key management team including the CEO.
- Payout ratio for taxable income has been consistently maintained at above the minimum 90% threshold for tax transparency.
- Has scaled up via DPU-accretive acquisitions from its sponsor's pipeline. The deal process is rigorous; involving a review by the board's audit committee, and if valued >5% of NAV, unit holders' approval at an EGM.
- The Suntec City AEI at SGD410m over four phases from 2012-15 resulted in a 14% increase in NLA and SGD848m or 18% increase in valuation at end-2016.
- Diversified into the UK, a new geography, in FY20 with the acquisition of Nova properties, a quality well-sited asset at a favourable valuation of 4.6% NPI yield versus comparable yields of 4.0-4.2%, based on recent market transactions.
- Ranked 38 out of 44 S-REITs in the independent 2021 Governance Index For Trusts Index, with lower governance and business risks scores versus peers.
- Leverage averaged c.37% from FY06-21, but has risen to c.43% after the Nova acquisition, which is the highest among peers.

<u>1Risk Rating & Score</u> - 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. <u>2Score Momentum</u> - 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. <u>3Controversy Score</u> - 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).

1. Financial highlights

Fig 1: Distributable income from operations turned positive QoQ

(SGD m)	3Q23	2Q24	3Q24	%QoQ	%YoY	9M23	9M24	9M24, % YoY
Gross revenue	123.4	117.1	117.7	1%	-5%	347.7	344.6	-1%
Property expenses	-38.8	-39.5	-37.9	-4%	-2%	-109.8	-113.8	4%
NPI	84.6	77.6	79.8	3%	-6%	237.9	230.8	-3%
JV income	23.8	24.9	25	0%	5%	70	74.7	7%
Distributable income from ops	46.2	44.0	44.7	n.m.	-100%			
Distributable income from capital	5.8	0.0	0.0	2%	-14%			
Total distributable income	52	44.0	44.7	3%	-12%	152.5	134.9	-12%
DPU (SGD cts)	1.793	1.531	1.58	1%	-5%	5.269	4.622	-12%
NAV per unit (SGD)	2.09	2.10	2.07	-1%	-1%			
Aggregate leverage (%)	42.7%	42.3%	42.3%	0%	-1%			
All-in financing cost (%)	3.78%	4.02%	4.06%	0%	0.28%			

Source: Company, Maybank IBG Research

2. Financial performance

Fig 2: Singapore portfolio continues to underpin portfolio performance

(SGD m)	3Q23	2Q24	3Q24	3Q24, %QoQ	3Q24, %YoY	9M23	9M24	9M24, % YoY
Gross revenue								
Singapore office	36.50	36.20	37.10	2%	2%	108.3	109.7	1%
Australia Portfolio	23.70	22.80	22.4	-2%	-5%	71.9	66.8	-7%
UK Portfolio	7.40	6.60	6.10	-8%	-18%	21.8	18.5	-15%
Singapore retail	33.50	35.00	35.20	1%	5%	99.2	104.5	5%
Suntec Convention	22.30	16.60	16.90	2%	-24%	46.5	45.1	-3%
NPI								
Singapore office	27.5	26.9	28.8	7%	5%	81.1	83	2%
Australia Portfolio	17.8	16.7	15.9	-5%	-11%	55.4	48.7	-12%
UK Portfolio	6.70	5.70	5.40	-5%	-19%	20.5	16.2	-21%
Singapore retail	22.80	25.10	24.30	-3%	7%	68	73	7%
Suntec Convention	7.80	3.20	5.40	69%	-31%	10.9	9.9	-9 %
JV Income								
Singapore office	15.5	17.9	16.9	-6%	9 %	45.8	50.3	10%
Australia Portfolio	0	1	0.4	-60%	n.m.	2.7	1.4	-48%
UK Portfolio	7.80	4.60	7.20	57%	-8%	22.2	19.6	-12%
Singapore retail	0.50	0.60	0.50	-17%	0%	1.4	1.6	14%
NPI margins (%)								Change YoY, ppt
Singapore office	75.3	74.3	77.6	3.3	2.3	74.9	75.7	0.8
Australia Portfolio	75.1	73.2	71.0	(2.3)	(4.1)	77.1	72.9	-4.1
UK Portfolio	90.5	86.4	88.5	2.2	(2.0)	94.0	87.6	-6.5
Singapore retail	68.1	71.7	69.0	(2.7)	1.0	68.5	69.9	1.3
Suntec Convention	35.0	19.3	32.0	12.7	(3.0)	23.4	22.0	-1.5

Source: Company, Maybank IBG Research

3. Operational highlights

Fig 3: Signs of improvement in its AU portfolio QoQ

	3Q23	1Q24	2Q24	3Q24	%QoQ	%YoY
NPI margin (%)	70.2	66.8	66.3	67.8	1.5	-2.4
SG Office rent reversion (%)	11.2	11.4	7.9	12.9	5	1.7
Suntec City rent reversion (%)	16.5	21.7	20.2	20.9	0.7	4.4
SG Office occupancy (%)	98.9	99.4	99.3	99.1	-0.2	0.2
AU Office occupancy (%)	97.3	88.9	89.1	90.6	1.5	-6.7
UK Office occupancy (%)	100	95.5	95.5	95.3	-0.2	-4.7
SG Retail occupancy (%)	98.3	95.8	95.6	98.3	2.7	0.0
Office occupancy						
Suntec City Office	100	99.4	100	99.9	-0.1	-0.1
One Raffles Quay	100	99.4	99.4	98.7	-0.7	-1.3
MBFC 1 & 2	95.5	99.2	97.4	97.5	0.1	2.0
177 Pacific Highway (Sydney)	100	100	100	100	0	0.0
Southgate Complex (Melbourne)	90.1	86.5	87.3	89.2	1.9	-0.9
477 Collins Street (Melbourne)	100	100	100	100	0	0.0
55 Currie Street (Adelaide)	100	56.2	56.2	61.4	5.2	-38.6
21 Harris Street (Sydney)	97.6	98.8	98.8	100	1.2	2.4
Nova (London)	100	100	100	99.6	-0.4	-0.4
Minister Building (London)	100	91.3	91.3	91.3	0	-8.7

Source: Company, Maybank IBG Research

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FYE 31 Dec	FY22A	FY23A	FY24E	FY25E	FY26E
Key Metrics					
Price/DPU(x)	15.5	17.2	17.7	16.5	16.0
P/BV (x)	0.6	0.6	0.6	0.6	0.6
P/NTA (x)	0.6	0.6	0.6	0.6	0.6
DPU yield (%)	6.4	5.8	5.6	6.1	6.2
FCF yield (%)	8.8	6.6	6.7	8.8	8.4
INCOME STATEMENT (SGD m)					
Revenue	427.3	462.7	467.1	481.7	487.0
Net property income	315.8	313.2	319.5	325.3	329.1
Management and trustee fees	(67.1)	(70.7)	(71.7)	(72.2)	(72.4)
Net financing costs	(151.4)	(174.7)	(158.3)	(150.9)	(145.6)
Associates & JV	144.9	36.0	104.1	104.3	104.6
Exceptionals	0.0	0.0	0.0	0.0	0.0
Other pretax income/expenses	0.0	0.0	0.0	0.0	0.0
Pretax profit	281.2	124.9	215.2	228.2	237.3
Income tax	(16.2)	(8.0)	(30.0)	(30.0)	(30.0)
Minorities	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Total return avail to unitholders	265.0	116.9	185.2	198.2	207.3
Core net profit	265.0	116.9	185.2	198.2	207.3
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BALANCE SHEET (SGD m)					
Cash & Short Term Investments	269.6	217.9	124.1	134.2	124.9
Accounts receivable	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	0.0	0.0	0.0	0.0	0.0
Inverstment properties	7,906.8	7,964.8	7,960.4	7,960.4	7,960.4
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	3,424.1	2,829.5	2,843.9	2,842.9	2,840.9
Other assets	110.0	117.0	107.3	108.3	107.8
Total assets	11,710.5	11,129.2	11,035.7	11,045.9	11,034.0
ST interest bearing debt	645.6	399.9	501.9	501.9	501.9
Accounts payable	128.7	120.0	120.2	120.1	120.2
LT interest bearing debt	4,197.9	3,860.5	3,733.9	3,733.9	3,733.9
Other liabilities	154.2	165.0	147.9	146.9	144.9
Total Liabilities	5,126.3	4,545.3	4,503.9	4,502.8	4,500.8
Shareholders Equity	6,464.4	6,455.8	6,403.9	4, <i>3</i> 02.8 6,415.2	6,405.3
Minority Interest	119.8	128.1	127.8	127.8	127.8
Total shareholder equity	6,584.2	6,583.9	6,531.8	6,543,1	6,533.1
Total liabilities and equity	11,710.5	11,129.2	11,035.7	11,045.9	11,034.0
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CASH FLOW (SGD m)					
Cash flow from operations	349.7	237.5	242.9	321.8	310.3
Capex	(0.2)	(1.5)	(1.5)	(1.5)	(1.5)
Acquisitions & investments	140.0	561.9	0.0	0.0	0.0
Disposal of FA & investments	0.0	0.0	0.0	0.0	0.0
Dividend income from associates	0.0	0.0	0.0	0.0	0.0
Other investing cash flow	0.0	0.0	0.0	0.0	0.0
CF from investing activities	139.8	560.4	(1.5)	(1.5)	(1.5)
Dividends paid	(263.4)	(209.7)	(205.0)	(212.2)	(225.6)
Interest expense	(133.1)	(171.2)	(158.3)	(150.9)	(145.6)
Change in debt	26.9	(603.0)	(24.6)	0.0	0.0
Equity raised / (purchased)	0.0	0.0	31.1	31.3	31.4
Other financial activities	(250.5)	(603.0)	21.6	21.6	21.6
CF from financing activities	(620.1)	(1,586.9)	(335.2)	(310.2)	(318.2)
Effect of exchange rate changes	(14.1)	(0.9)	0.0	0.0	(0.0012)
Net cash flow	(14.7)	(789.8)	(93.7)	10.1	(9.4)

FYE 31 Dec	FY22A	FY23A	FY24E	FY25E	FY26E
Key Ratios					
Growth ratios (%)					
Revenue growth	19.3	8.3	0.9	3.1	1.1
Net property income growth	24.0	(0.8)	2.0	1.8	1.2
Core net profit growth	52.3	(55.9)	58.4	7.0	4.6
Distributable income growth	na	na	na	na	na
Profitability ratios (%)					
Net property income margin	73.9	67.7	68.4	67.5	67.6
Core net profit margin	62.0	25.3	39.7	41.1	42.6
Payout ratio	96.0	176.2	109.2	110.9	110.3
DuPont analysis					
Total return margin (%)	62.0	25.3	39.7	41.1	42.6
Gross revenue/Assets (x)	0.0	0.0	0.0	0.0	0.0
Assets/Equity (x)	1.8	1.7	1.7	1.7	1.7
ROAE (%)	na	na	na	na	na
ROAA (%)	2.3	1.0	1.7	1.8	1.9
Leverage & Expense Analysis					
Asset/Liability (x)	2.3	2.4	2.5	2.5	2.5
Net gearing (%) (excl. perps)	69.5	61.4	62.9	62.7	62.9
Net interest cover (x)	1.9	1.5	1.7	1.8	1.9
Debt/EBITDA (x)	16.8	16.2	15.7	15.4	15.2
Capex/revenue (%)	0.0	0.3	0.3	0.3	0.3
Net debt/ (net cash)	4,573.9	4,042.4	4,111.6	4,101.5	4,110.9
Debt/Assets (x)	0.41	0.38	0.38	0.38	0.38

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 DZULKAFLI 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.thuhuong@maybank.com

LEE Jia Yu (65) 6231 5843 jiayu.lee@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, CFA (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) 6231 5831 winsonphoon@maybank.com

PORTFOLIO STRATEGY ONG Seng Yeow (65) 6231 5839

(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

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

Anand PATHMAKANTHAN (603) 2297 8783 anand.pathmakanthan@maybank-ib.com • Equity Strategy

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

Nur Natasha ARIZA (603) 2297 8691 natashaariza.aizarizal@maybank-ib.com • Healthcare

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

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

SINGAPORE

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

Eric ONG (65) 6231 5849 ericong@maybank.com • Healthcare • Transport • SMIDs

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

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

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

Hussaini SAIFEE (65) 6231 5837 hussaini.saifee@maybank.com • Telcos • Internet

PHILIPPINES

Kervin Laurence SISAYAN Head of Research (63) 2 5322 5005 kervin.sisayan@maybank.com • Strategy • Banking & Finance • Telcos

Daphne SZE (63) 2 5322 5008 daphne.sze@maybank.com • Consumer

Raffy MENDOZA (63) 2 5322 5010 joserafael.mendoza@maybank.com • Property • REITs • Gaming

Michel ALONSO (63) 2 5322 5007 michelxavier.alonso@maybank.com • Conglomerates

Germaine GUINTO (63) 2 5322 5006 germaine.guinto@maybank.com • Utilities

Ronalyn Joyce LALIMO (63) 2 5322 5009 rona.lalimo@maybank.com • SMIDs

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

INDONESIA

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

Willy GOUTAMA (62) 21 8066 8688 willy.goutama@maybank.com • Consumer

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

Paulina MARGARETA (62) 21 8066 8690 paulina.tjoa@maybank.com • Autos • Healthcare

Jocelyn SANTOSO (62) 21 8066 8689 jocelyn.santoso@maybank.com • Consumer

Hasan BARAKWAN (62) 21 8066 2694 hasan.barakwan@maybank.com • Metals & Mining • Oil & Gas

Faiq ASAD (62) 21 8066 8692 faiq.asad@maybank.com • Banking & Finance

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

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

Boonyakorn AMORNSANK (66) 2658 5000 ext 1394 boonyakorn.amornsank@maybank.com • Services

Nontapat SAHAKITPINYO (66) 2658 5000 ext 2352 nontapat.sahakitpinyo@maybank.com • Healthcare

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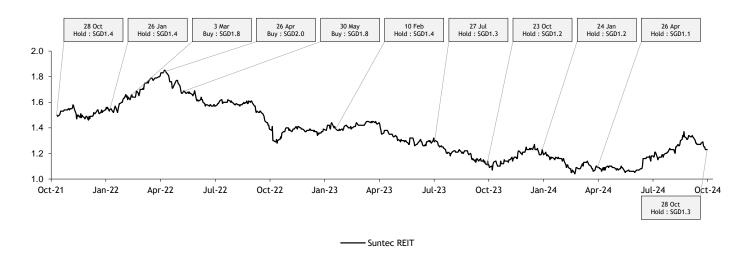
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🌏 Malaysia

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

📀 Sales Trading

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

Philippines Keith Roy keith_roy@maybank.com Tel: (63) 2 5322 3184 📀 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 Greg Smith gsmith@maybank.com 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

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