

RCE Capital Bhd (RCE MK)

Cautious ahead of civil service salary hike in December

Maintain HOLD with a tad lower TP of MYR1.45 (-3%)

We met senior management to discuss RCE's outlook. Financing receivables growth will be muted until the civil service salary hike. Credit cost ratios also remain elevated. We trim our EPS estimates by 1-2% and TP to MYR1.45 from MYR1.50 (MYR3.00 pre-1-for-1 bonus issue) on lower end-FY25E P/BV of 2.4x from 2.5x due to our slightly lower earnings estimates. On another note, we update our ESG 2.0 analysis of RCE with a slightly higher score of 75/100 (71/100 previously).

Financing receivables growth subdued for now

Recall that 1QFY3/25 financing receivables eased 1% QoQ (Fig. 1). RCE reiterated that it is disbursing fewer new financings as the credit quality of new applicants have been less than desirable. Ostensibly, many accumulated massive debts through 'compressed' financing where they borrowed from multiple financial institutions nearly simultaneously. RCE also stated that the industry is also seeing the entry of more aggressive competitors who have been more lax in their credit policy.

Credit cost ratios also remain elevated

At the same time, RCE stated that the level of resignations and early retirements among civil servants have not normalised despite the upcoming civil service salary hike in December. Although the government has committed to raise the salaries of civil servants by an average of 15% over 2 years, we understand that many are still opting to leave the civil service for the private sector due to more attractive salaries offered by the latter and thereby, causing credit cost ratios to remain high (Fig. 2).

Trim EPS estimates by 1-2% only though

Notwithstanding, RCE stated that its outlook will improve once the civil service salary hike takes effect. We forecast its financing receivables to grow by a matching 15% over 2 years from December. We only raise our credit cost ratio forecasts to 1.5% from 1.3% and trim FY25E/FY26E/FY27E EPS by 2%/2%/1%. Dividend yields of >5% p.a. ought to support its share price, in our view. The next key lookout is Budget 2025 on 18 Oct where more details on the civil service salary hike will be revealed.

FYE Mar (MYR m)	FY23A	FY24A	FY25E	FY26E	FY27E
Operating income	261	281	296	319	335
Pre-provision profit	213	215	227	246	258
Core net profit	139	139	147	159	167
Core FDEPS (MYR)	0.09	0.09	0.10	0.11	0.11
Core FDEPS growth(%)	3.7	(0.0)	4.5	8.3	5.0
Net DPS (MYR)	0.15	0.08	0.08	0.09	0.09
Core FD P/E (x)	9.7	14.2	15.5	14.4	13.7
P/BV (x)	1.7	2.4	2.6	2.5	2.4
Net dividend yield (%)	16.5	5.6	5.2	5.6	5.9
Book value (MYR)	0.55	0.57	0.59	0.61	0.63
ROAE (%)	16.5	17.0	17.4	18.1	18.3
ROAA (%)	4.9	4.7	4.8	4.9	4.9
Consensus net profit	-	-	148	158	166
MIBG vs. Consensus (%)	-	-	(0.9)	0.5	0.5

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

HOLD

Share Price	MYR 1.53
12m Price Target	MYR 1.45 (-0%)
Previous Price Target	MYR 1.50

Company Description

RCE Capital is principally involved in the provision of general financing services.

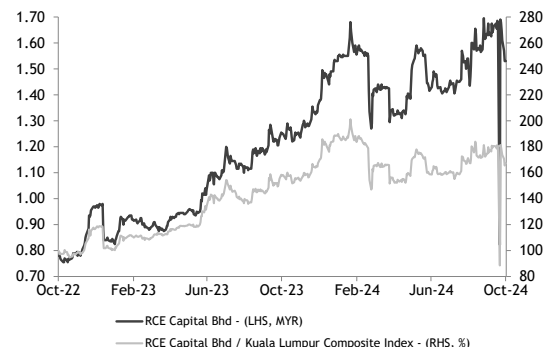
Statistics

52w high/low (MYR)	1.70/0.82
3m avg turnover (USDm)	0.3
Free float (%)	34.0
Issued shares (m)	1,482
Market capitalisation	MYR2.3B USD543M

Major shareholders:

Cempaka Empayar Sdn. Bhd.	57.9%
Khai Yoon Woo	1.5%
Employees Provident Fund	1.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(6)	6	22
Relative to index (%)	(4)	4	6

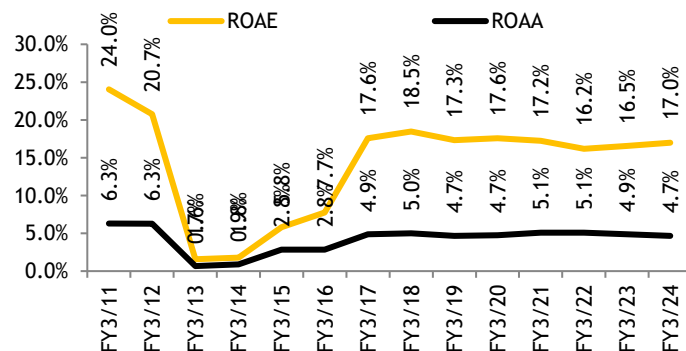
Source: FactSet

ESG@MAYBANK IBG
Tear Sheet Insert

Value Proposition

- RCE Capital provides personal financing, the ultimate customers being civil servants.
- With a gross financing balance of just MYR2.1b, we estimate that its market share is only 2%.
- Non-performing financing kept in check thanks to nondiscretionary direct salary deductions.
- Competitive advantage lies in fast financing processing turnaround time of 48 hours.
- ROE generation surpasses that of the average for the overall banking industry.

ROAE and ROAA

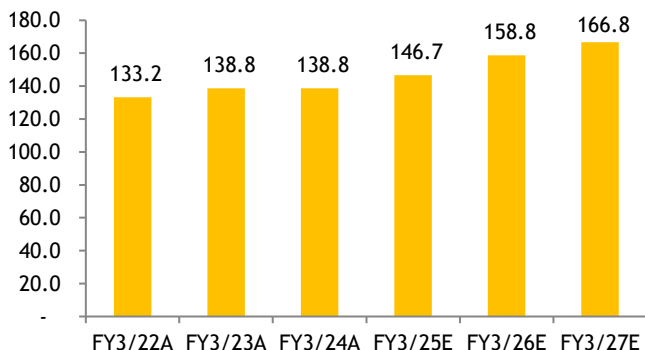


Source: Company

Financial Metrics

- Introduced better credit scoring model in 2013. We forecast gross financing CAGR of 6% p.a. over the next three years.
- Average cost of funds is rising but so is average financing yields.
- Asset quality better than before. New financings are smaller in size (<2%).
- Forecast stable 3-year forward core net profit CAGR of 6% p.a.
- Recently raised dividend payout ratio policy from 20-40% to 60-80%.

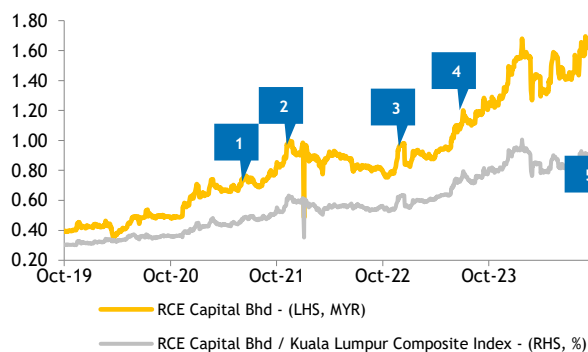
Core net profit (MYRm)



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

Price Drivers

Historical share price trend



Source: Company, Maybank IBG Research

1. 2QFY21 net profit grew 21% YoY to a record high of MYR33.0m.
2. Announced share DPS of 1 treasury share for 20 shares held and bonus issue of 19 shares for 21 shares held.
3. Announced a huge special DPS of 18sen and higher-than expected interim DPS of 5sen.
4. Announced that it raised its dividend policy from 20-40% DPR to 60-80% DPR.
5. Share price went ex- following its 1-for-1 bonus issue.

Swing Factors

Upside

- Easing competition - competitors have been reducing their exposure to personal financing.
- Lower cost of funds - we estimate that every 25bps reduction in cost of funds will accrete 3% to earnings.
- Access to CCRIS - if RCE Capital gains access to CCRIS, it can better assess customers' total indebtedness

Downside

- High household debt - Household debt to GDP is elevated at >80% and may crimp customers' repayment ability.
- Need to leverage - RCE Capital cannot take deposits and thus, has to assume debt to finance its financing.
- Asset-liability duration mismatch - customers' repayment may not match RCE's debt repayment.

samuel.y@maybank-ib.com

Risk Rating & Score ¹	N/A
Score Momentum ²	N/A
Last Updated	N/A
Controversy Score ³	N/A

Business Model & Industry Issues

- Being a non-bank financial institution (NBFI), RCE does not have a large environmental footprint. That said, we opine that it has a large social footprint by way of responsible financing.
- NBFIs were a lot more carefree in disbursing financing before Jul 2013. In Jul 2013, Bank Negara Malaysia instituted macro prudential measures to rein in high household debt levels caused by the aforementioned.
- Since then, reflecting RCE's broad transition to more socially-responsible lending parameters, tenure of its financing is capped at 10 years (25 years previously) and debt service ratio of its customers is capped at 60%.
- In CY13, RCE also put in place an in-house credit scoring model that precludes RCE from over-lending to particular customers. As a result, average financing/customer has eased from c. MYR30,000 in FY3/13 to c. MYR20,000 currently.
- To be sure, RCE does carry out related party transactions (RPT) as it places deposits and borrows from AMMB Holdings which is 12%-owned by Tan Sri Azman Hashim, the controlling shareholder of RCE.
- That said, interest rates on the aforementioned deposits and borrowings do not appear unfair to us or detrimental to minority shareholders. RCE has also been a constituent of the FTSE4Good Bursa Malaysia Index since 22 Jun 2020.
- All in all, we rate RCE's ESG credentials vis-à-vis its core business as commendable. RCE scores above-average in our proprietary scoring methodology with an overall score of 75/100 (71/100 previously).

Material E issues

- No major environmental issues. Cut paper utilisation/employee by 10% to 5.4k pieces in FY3/24 vis-à-vis FY3/20.
- The above was achieved via emails reminding employees to "Think before you Print" and printing on both sides.
- FY3/24 scope 1 and 2 emissions in CO2e tonnes per employee cut to 0.85 (FY3/20: 0.96).
- Part of the reason for the above is due to the extensive use of energy saving light bulbs.

Material S issues

- RCE is guided by Bank Negara Malaysia's (BNM) guidelines for responsible financing.
- In Jul 2013, BNM instituted macro prudential measures to rein in high household debt levels.
- Since then, tenure of its financing is capped at 10 years and debt service ratio of its customers is capped at 60%.
- In-house credit scoring model put in place in CY13 precludes RCE from over-lending to a customer.
- As a result, average financing/customer has eased from c. MYR30,000 in FY3/13 to c. MYR20,000 currently.
- Technical and soft skills trainings provided to sales team to promote responsible financing.
- Extends study grants to students pursuing the Association of Chartered Certified Accountants qualification.
- To date, RCE has extended MYR584,000 in study grants to 36 students.
- An overwhelming 74% of RCE's employees as at end-FY3/24 are women.
- FY3/24 overall employee turnover rate decreased to 12.8% (FY3/23: 16.0%, FY3/22: 17.5%).
- FY3/24 average training hours per employee was 24 (FY3/23: 35, FY3/22: 24).

Key G metrics and issues

- BOD comprises 1 Non-Independent Non-Executive Chairman (NINEC), 3 Non-Independent Non-Executive Directors (NINED) and 4 Independent Directors (ID; 50% of total).
- Largest shareholder is Cempaka Empayar Sdn Bhd, which is controlled by Tan Sri Azman Hashim (TSAH).
- NINEC, Shahman Azman is a son of TSAH. NINED, Shalina Azman is a daughter of TSAH.
- Only 2 of the 8 BOD members are women (25% representation), the aforementioned Shalina Azman and Azura Binti Rahman.
- FY3/24 directors' remuneration accounted for <1% of FY3/24 net profit.
- Deloitte PLT is the independent auditor. They have been appointed for >10 years.
- There are 4 BOD level committees. 2 are chaired by IDs (i.e. Audit and Nomination & Remuneration), 1 chaired by a NINED (i.e. Employees' Share Scheme) and 1 chaired by the NINEC (i.e. Sustainability Management).
- Carries out RPTs with AMMB Holdings (AMMB), which is 12%-owned by TSAH. As at end-FY3/24, RCE has deposits of MYR396.2m and borrowings of MYR379.9m with AMMB.
- That said, interest rates on the aforementioned deposits and borrowings appear fair to us.
- RCE hired PricewaterhouseCoopers Consulting to review its related party transactions.

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).

Quantitative Parameters (Score: 50)						
	Particulars	Unit	2022	2023	2024	ACSM MK (FY3/24)
E	Scope 1 emissions	tCO2e	16	19	22	200
	Scope 2 emissions	tCO2e	150	155	152	2,317
	Total	tCO2e	166	174	174	2,517
	Scope 3 emissions	tCO2e	N/A	N/A	377	N/A
	Total	tCO2e	166	174	551	2,517
	Scope 1 & 2 emissions per employee	tCO2e	0.94	0.90	0.85	0.81
	Energy consumption	GJ	1,206.6	1,300.8	1,339.9	N/A
	Water consumption	m3	N/A	N/A	267	19,457
	Paper consumption per employee	'000 pieces	3.7	3.7	5.4	N/A
	Waste generated	kg	N/A	N/A	N/A	N/A
Waste diverted from disposal	kg	322.4	796.7	1,010.7	N/A	
S	% of women in workforce	%	73%	74%	74%	66%
	% of women in managerial roles	%	64%	66%	69%	39%
	Sales team responsible financing training rate	%	100.0%	100.0%	97.2%	N/A
	Responsible financing articles posted on social media	posts	7	19	7	N/A
	Complaints received & resolved	number	7	6	8	N/A
	Employee turnover rate	%	17.5	16.0	12.8	18.2
Employee training per employee	hours	24	35	24	21	
G	Incidents of non-compliance	incidents	1	3	-	-
	Board salary as % of core net profit	%	0.7%	0.7%	0.7%	1.1%
	Independent directors on the Board	%	50%	50%	50%	56%
	% of profits returned to shareholders	%	57%	158%	79%	34%
Female directors on the Board	%	11%	13%	25%	44%	

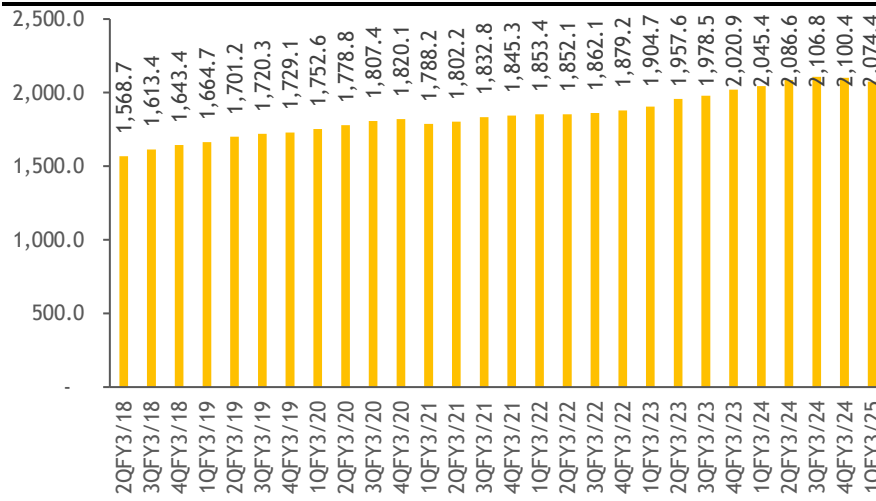
Qualitative Parameters (Score: 100)	
a) Is there an ESG policy in place and whether there is a standalone ESG committee or is it part of a risk committee?	<i>Yes. RCE has an ESG policy in place. It has a Sustainability Working Committee which reports to the Sustainability Management Committee which in turn, reports directly to the Board of Directors.</i>
b) Is the senior management salary linked to fulfilling ESG targets?	<i>Yes.</i>
c) Does the company follow the task force of climate related disclosures (TCFD) framework for ESG reporting?	<i>Yes.</i>
e) Does the company have a mechanism to capture Scope 3 emissions - which parameters are captured?	<i>Yes. Employee commute.</i>
f) What are the 2-3 key carbon mitigation/water/waste management strategies adopted by the company?	<i>Switching off all office lights and equipment during breaks and before leaving office, retro-fitting LED lighting, recycling paper and avoiding unnecessary printing.</i>
g) Does carbon offset form part of the net zero/carbon neutrality target of the company?	<i>No, as RCE is not a major polluter.</i>

Target (Score: 100)		
Particulars	Target	Achieved
Reduce GHG emissions/employee by FY3/24E	1.0	0.9
Women representation on board by FY3/25E	30%	NA
Impact		
NA		
Overall Score: 75		
As per our ESG matrix, RCE Capital (RCE MK) has an overall score of 75.		

ESG score	Weights	Scores	Final Score
Quantitative	50%	50	25
Qualitative	25%	100	25
Target	25%	100	25
Total			75

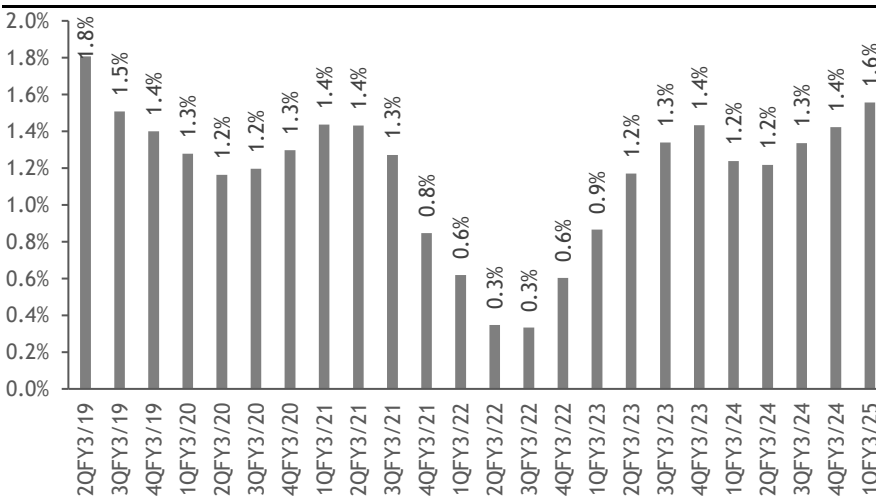
As per our ESG assessment, RCE has an established framework, internal policies, and tangible mid/long-term targets. RCE's overall ESG score is 75, which makes its ESG rating above average in our view (average ESG rating = 50; refer to Appendix I for our ESG Assessment Scoring).

Figure 1: Gross financing receivables (MYRm)



Source: Company

Figure 2: Trailing 12 months credit cost ratio



Source: Company, MIBG Research

Appendix I

Methodology of our proprietary ESG scoring methodology.

We evaluate the ESG ratings based on quantitative, qualitative and ESG targets. We assign a score for each of these three parameters. The overall rating is based on the weighted average of the scores: quantitative (50%), qualitative (25%) and ESG target (25%).

For the quantitative, qualitative and ESG target, the sub-parameters are assigned a score - '0' for data not available, '+1' for improving trajectory, positive change, 'Yes', better than peers or a positive number if historical is not available and '-1' for declining trajectory, negative change, 'No', lower than peers or a negative number. The total of the scores of all the sub-parameters is divided by the total number of sub-parameters, to derive the score of each of the three parameters.

The sub-parameters may be different for different industries depending on the key areas to monitor for each industry. A company should achieve a minimum score of 50 for an average ESG rating.

FYE 31 Mar	FY23A	FY24A	FY25E	FY26E	FY27E
Key Metrics					
Core P/E (x)	9.6	14.2	15.3	14.1	13.4
Core FD P/E (x)	9.7	14.2	15.5	14.4	13.7
P/BV (x)	1.7	2.4	2.6	2.5	2.4
P/NTA (x)	1.8	2.5	2.8	2.7	2.5
Net dividend yield (%)	16.5	5.6	5.2	5.6	5.9
INCOME STATEMENT (MYR m)					
Islamic banking income	209.4	221.2	233.0	250.5	265.3
Other income	52.0	59.6	62.6	68.7	70.1
Total non-interest income	261.4	280.8	295.5	319.2	335.4
Operating income	261.4	280.8	295.5	319.2	335.4
Staff costs	(27.1)	(32.2)	(33.6)	(36.3)	(38.2)
Other operating expenses	(21.7)	(33.6)	(34.9)	(37.4)	(39.1)
Operating expenses	(48.8)	(65.8)	(68.6)	(73.7)	(77.3)
Pre-provision profit	212.6	215.1	227.0	245.5	258.1
Other allowances	(28.7)	(30.2)	(31.6)	(34.0)	(35.9)
Associates & JV income	0.0	0.0	0.0	0.0	0.0
Pretax profit	183.9	184.8	195.4	211.6	222.2
Income tax	(45.2)	(46.1)	(48.7)	(52.8)	(55.4)
Reported net profit	138.8	138.8	146.7	158.8	166.8
Core net profit	138.8	138.8	146.7	158.8	166.8
BALANCE SHEET (MYR m)					
Cash & deposits with banks	879.7	840.2	876.3	925.5	964.2
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	0.0	0.0	0.0	0.0	0.0
Dealing securities	0.0	0.0	0.0	0.0	0.0
Available-for-sale securities	0.0	0.0	0.0	0.0	0.0
Investment securities	0.0	0.0	0.0	0.0	0.0
Financing and advances	1,953.3	2,027.3	2,126.0	2,333.1	2,378.7
Fixed assets	7.2	7.3	7.0	6.6	6.3
Intangible assets	47.3	47.3	47.3	47.3	47.3
Other assets	59.3	73.5	73.5	73.5	73.5
Total assets	2,946.8	2,995.6	3,130.1	3,386.1	3,470.0
Derivatives financial instruments	0.0	0.0	0.0	0.0	0.0
Subordinated debt	0.0	0.0	0.0	0.0	0.0
Other securities in issue	1,290.9	1,175.8	1,175.8	1,175.8	1,175.8
Other borrowings	434.3	552.9	657.6	878.7	927.3
Other liabilities	416.0	437.1	437.5	438.2	438.7
Total liabilities	2,141.2	2,165.8	2,270.9	2,492.7	2,541.8
Share capital	201.9	201.9	201.9	201.9	201.9
Reserves	603.7	627.9	657.3	691.5	726.3
Shareholders' funds	805.7	829.8	859.2	893.4	928.2
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	0.0
Total equity	805.7	829.8	859.2	893.4	928.2
Total liabilities & equity	2,946.8	2,995.6	3,130.1	3,386.1	3,470.0

FYE 31 Mar	FY23A	FY24A	FY25E	FY26E	FY27E
Key Ratios					
Growth (%)					
Net interest income	na	na	na	na	na
Non-interest income	9.2	7.4	5.2	8.0	5.1
Operating expenses	(3.6)	34.9	4.3	7.5	5.0
Pre-provision profit	12.6	1.2	5.5	8.2	5.1
Core net profit	4.2	(0.0)	5.7	8.3	5.0
Gross loans	7.5	3.9	5.0	10.0	2.0
Customer deposits	na	na	na	na	na
Total assets	8.1	1.7	4.5	8.2	2.5
Profitability (%)					
Non-int. income/Total income	100.0	100.0	100.0	100.0	100.0
Cost/income	18.7	23.4	23.2	23.1	23.1
Liquidity (%)					
Loans/customer deposits	na	na	na	na	na
Asset quality (%)					
Gross NPF	3.8	4.0	4.0	4.0	4.0
Capital adequacy (%)					
CET1	na	na	na	na	na
Tier 1 capital	na	na	na	na	na
Risk-weighted capital	na	na	na	na	na
Returns (%)					
ROAE	16.5	17.0	17.4	18.1	18.3
ROAA	4.9	4.7	4.8	4.9	4.9
Shareholders equity/assets	27.3	27.7	27.4	26.4	26.8

Source: Company; Maybank IBG Research

Research Offices

ECONOMICS

Suhaimi ILIAS
Chief Economist
Malaysia | Philippines | Global
(603) 2297 8682
suhaimi_iliasmaybank-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
alantau@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
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
joseraphael.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

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

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

THAILAND

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

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

Wasu MATTANAPOTCHANART
(66) 2658 5000 ext 1470
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 AMORNANK
(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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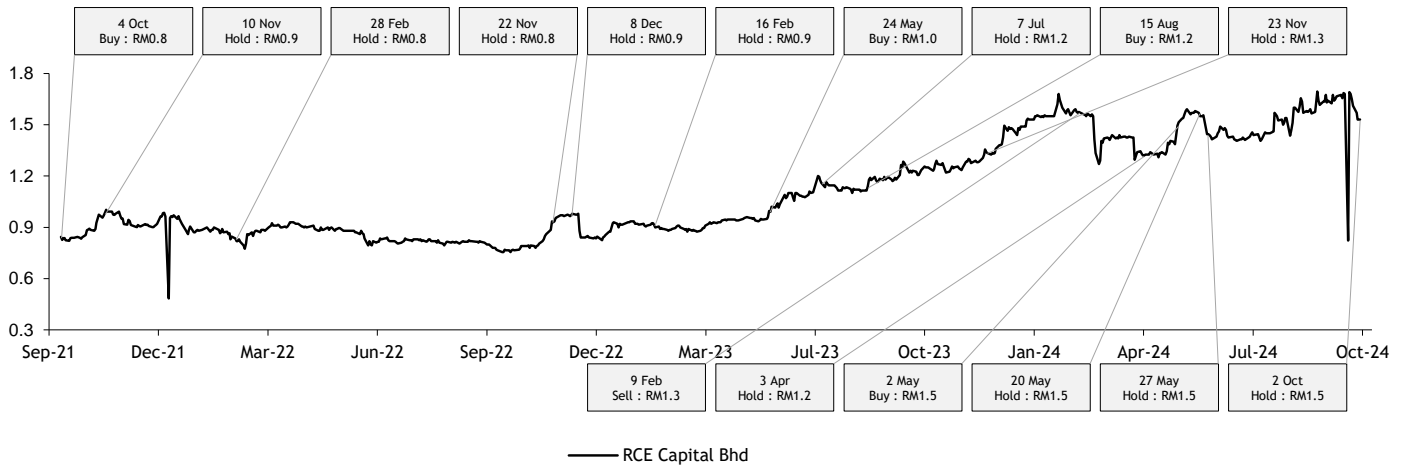
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Malaysia

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

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
Tel: (62) 21 2557 1188

Philippines

Keith Roy
keith_roy@maybank.com
Tel: (63) 2 5322 3184

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