

# SATS (SATS SP)

Share Price: SGD3.80

Target Price: SGD3.82 (+1%)

MCap (USD): 3.0B

ADTV (USD): 5M

Singapore

Aviation

# HOLD

 (Unchanged)

## Solid earnings

- 2Q16 in line. Solid earnings on strong margin expansion.
- Beneficiary of a pick-up in air traffic. TFK to turn profitable.
- Maintain HOLD. Raise TP to SGD3.82 from SGD3.21 on EPS upgrade and higher target multiple.

### Productivity efforts drove margin expansion

2QFY3/16 net income of SGD59.7m (+26.8% YoY, +20.4% QoQ) was in line with 1H16 at 49% of our full-year estimates. Revenue decline was due to the transfer of its food distribution business to thenew JV, which roughly broke even. EBITDA margin expanded by a strong 4.6ppt to 18.0% as it benefited from productivity efforts and lower raw material costs. Management sees acquiring an effective 34.3% stake in Brahim's inflight catering business as an opportunity to participate in Malaysia's aviation growth story, but declined to discuss details pending deal completion. It cautions that the current operating environment remains challenging.

### Benefits from uptick in traffic; TFK to turn profitable

With oil prices staying low, we expect the impending decline in air ticket prices to stimulate travel demand and lift air traffic. SATS's margins should expand as it benefits from positive operating leverage. We also expect TFK Corp, its inflight catering unit in Japan, to turn profitable in 2H16 on market consolidation and workload increase from new customer Delta Air from Oct 2015.

### TP raised on EPS upgrade and higher target multiple

We raise our TP to SGD3.82 (from SGD3.21) after tweaking our EPS estimates and assigning a higher target multiple. We raise FY16-18E EPS estimates by 1.5%-2.6% on positive operating leverage as workload should increase in the year ahead. We also roll forward our valuation basis to FY3/17E EPS and assign a higher target multiple of 18x (1SD above 10-year average) from 16x as we expect the market to reward the stock for its solid earnings growth profile. However, upside to the share price appears limited and we will look to accumulate at a better entry point. Maintain HOLD.

FYE Mar (SGD m)	FY14A	FY15A	FY16E	FY17E	FY18E
Revenue	1,786.7	1,753.2	1,757.2	1,833.7	1,890.9
EBITDA	248.2	246.2	287.8	303.1	312.6
Core net profit	183.0	195.9	227.2	234.5	242.2
Core EPS (cts)	16.4	17.6	20.6	21.2	21.9
Core EPS growth (%)	(9.8)	7.5	16.7	3.2	3.3
Net DPS (cts)	13.0	14.0	15.0	16.0	17.0
Core P/E (x)	23.2	21.6	18.5	17.9	17.3
P/BV (x)	3.0	2.9	2.8	2.7	2.5
Net dividend yield (%)	3.4	3.7	3.9	4.2	4.5
ROAE (%)	13.0	13.7	15.4	15.2	15.0
ROAA (%)	9.1	9.7	11.3	11.4	11.3
EV/EBITDA (x)	13.2	13.0	14.0	13.2	12.7
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash

### Key Data

52w high/low (SGD)	4.05/2.85
3m avg turnover (USDm)	5.0
Free float (%)	54.9
Issued shares (m)	1,124
Market capitalization	SGD4.3B
Major shareholders:	
-Temasek Holdings Pte Ltd. (Investment C	42.6%
-Capital Research & Management Co. (Glo	2.2%
-Aberdeen Asset Management (Asia) Ltd.	2.0%

### Share Price Performance



	1 Mth	3 Mth	12 Mth
Absolute(%)	(4.0)	0.5	23.0
Relative to index (%)	(11.8)	5.5	32.7

### Maybank vs Market

	Positive	Neutral	Negative
Market Recs	2	4	0
<b>Maybank Consensus</b>			
Target Price (SGD)	3.82	3.84	(0.5)
'16 PATMI (SGDm)	227	211	7.7
'17 PATMI (SGDm)	235	231	1.6

Source: FactSet; Maybank

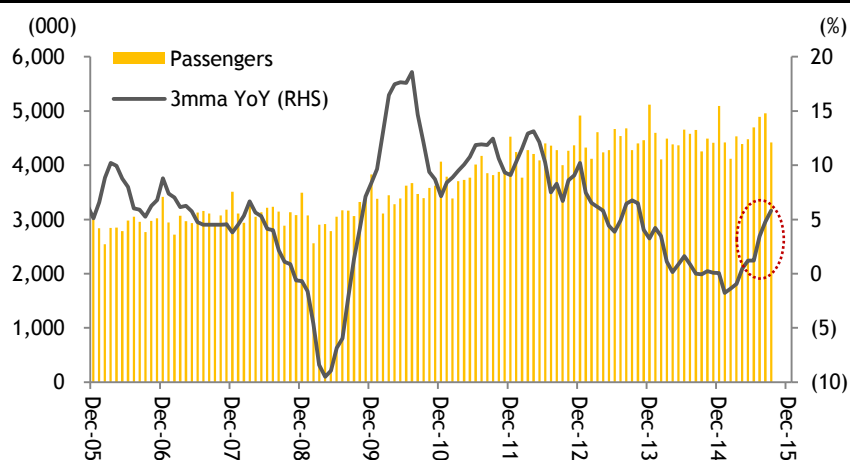
Derrick Heng, CFA  
(65) 6231 5843  
derrickheng@maybank-ke.com.sg

Figure 1: Quarterly profit and loss

FYE 31 Mar	2Q15	1Q16	2Q16	Change		YTD16	% of FY	FY16E
	(SGD m)	(SGD m)	(SGD m)	(QoQ %)	(YoY %)	(SGD m)		(SGD m)
Revenue	442.2	416.9	422.7	1.4	(4.4)	839.6	45.8	1,832.2
EBITDA	59.4	61.3	76.2	24.3	28.3	137.5	48.4	283.8
D&A	(16.9)	(17.3)	(17.0)	(1.7)	0.6	(34.3)	49.7	(69.0)
EBIT	42.5	44.0	59.2	34.5	39.3	103.2	48.0	214.8
Net interest income/(expense)	0.1	0.6	0.4	(33.3)	>100	1.0	182.0	0.5
Other items	0.2	2.5	0.0	n.m.	n.m.	2.5	n.m.	0.0
Associates & JVs	10.8	12.8	11.9	(7.0)	10.2	24.7	45.7	54.0
PBT	53.6	59.9	71.5	19.4	33.4	131.4	48.8	269.4
Taxation	(7.9)	(11.3)	(12.1)	7.1	53.2	(23.4)	54.2	(43.2)
MI	1.4	1.0	0.3	(70.0)	(78.6)	1.3	(27.7)	(4.7)
Net Income	47.1	49.6	59.7	20.4	26.8	109.3	49.3	221.5

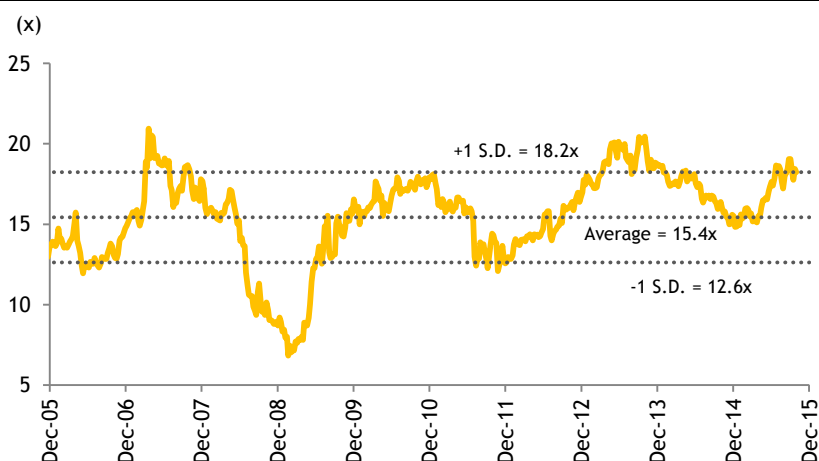
Source: Company, Maybank KE

Figure 2: Changi Airport's passenger traffic is rebounding



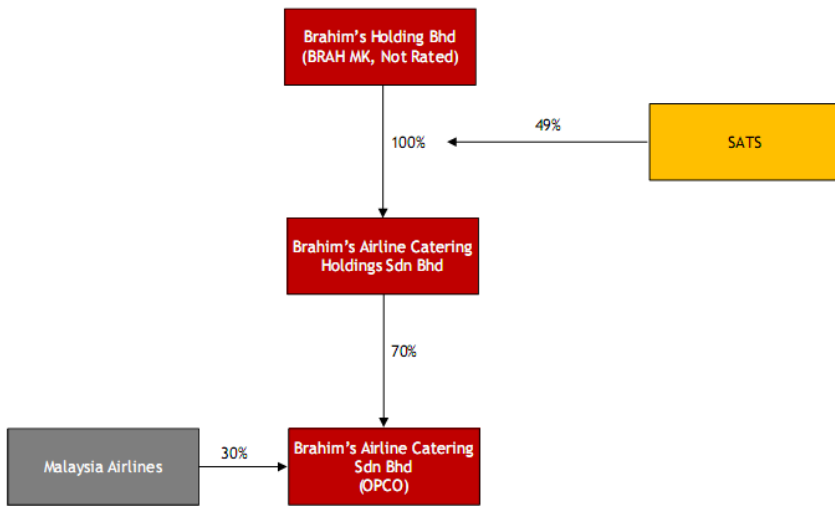
Source: Changi Airport Group

Figure 3: Forward P/E



Source: Bloomberg, Maybank KE

Figure 4: SATS is taking an effective 34.3% stake in Brahim's inflight catering business



Source: Company, Maybank KE

FYE 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
<b>Key Metrics</b>					
P/E (reported) (x)	23.5	21.6	18.5	17.9	17.3
Core P/E (x)	23.2	21.6	18.5	17.9	17.3
P/BV (x)	3.0	2.9	2.8	2.7	2.5
P/NTA (x)	3.5	3.3	3.1	3.0	2.8
Net dividend yield (%)	3.4	3.7	3.9	4.2	4.5
FCF yield (%)	5.2	6.3	2.2	5.0	5.2
EV/EBITDA (x)	13.2	13.0	14.0	13.2	12.7
EV/EBIT (x)	19.1	18.0	18.4	17.1	16.3

**INCOME STATEMENT (SGD m)**

Revenue	1,786.7	1,753.2	1,757.2	1,833.7	1,890.9
EBITDA	248.2	246.2	287.8	303.1	312.6
Depreciation	(77.2)	(68.2)	(69.0)	(69.1)	(69.1)
EBIT	171.0	178.0	218.8	234.0	243.6
Net interest income / (exp)	(1.8)	0.4	0.5	0.2	(0.1)
Associates & JV	47.2	48.1	54.0	55.1	56.2
Exceptionals	(2.6)	(0.2)	0.0	0.0	0.0
Other pretax income	1.7	(1.5)	2.5	0.0	0.0
Pretax profit	215.5	224.8	275.9	289.3	299.7
Income tax	(33.4)	(34.1)	(44.0)	(48.0)	(50.0)
Minorities	(1.7)	5.0	(4.8)	(6.8)	(7.4)
Reported net profit	180.4	195.7	227.2	234.5	242.2
Core net profit	183.0	195.9	227.2	234.5	242.2

**BALANCE SHEET (SGD m)**

Cash & Short Term Investments	340.8	410.9	346.6	388.2	427.8
Accounts receivable	287.5	282.6	288.9	301.4	310.8
Inventory	46.3	18.7	48.3	50.3	51.9
Reinsurance assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equip (net)	567.9	551.7	552.7	552.6	552.6
Intangible assets	185.0	165.5	165.5	165.5	165.5
Investment in Associates & JVs	494.8	464.8	489.1	513.9	539.2
Other assets	97.5	125.5	125.5	125.5	125.5
<b>Total assets</b>	<b>2,019.8</b>	<b>2,019.7</b>	<b>2,016.6</b>	<b>2,097.5</b>	<b>2,173.3</b>
ST interest bearing debt	17.6	15.6	15.6	15.6	15.6
Accounts payable	267.3	287.3	209.3	218.1	224.8
Insurance contract liabilities	0.0	0.0	0.0	0.0	0.0
LT interest bearing debt	96.6	89.7	89.7	89.7	89.7
Other liabilities	124.0	110.0	110.0	110.0	110.0
<b>Total Liabilities</b>	<b>505.4</b>	<b>502.1</b>	<b>424.1</b>	<b>432.9</b>	<b>439.6</b>
Shareholders Equity	1,416.8	1,441.1	1,513.5	1,582.3	1,647.7
Minority Interest	97.6	76.5	78.9	82.3	86.0
<b>Total shareholder equity</b>	<b>1,514.4</b>	<b>1,517.6</b>	<b>1,592.4</b>	<b>1,664.6</b>	<b>1,733.7</b>
<b>Total liabilities and equity</b>	<b>2,019.8</b>	<b>2,019.7</b>	<b>2,016.6</b>	<b>2,097.5</b>	<b>2,173.3</b>

**CASH FLOW (SGD m)**

Pretax profit	215.5	224.8	275.9	289.3	299.7
Depreciation & amortisation	77.2	68.2	69.0	69.1	69.1
Adj net interest (income)/exp	1.8	(0.4)	(0.5)	(0.2)	0.1
Change in working capital	35.0	21.3	(113.8)	(5.9)	(4.2)
Cash taxes paid	(38.5)	(35.3)	(44.0)	(48.0)	(50.0)
Other operating cash flow	0.0	0.0	0.0	0.0	0.0
Cash flow from operations	249.8	237.5	132.5	249.3	258.4
Capex	(56.5)	(60.8)	(70.0)	(69.0)	(69.1)
Free cash flow	220.5	265.4	92.2	210.6	220.2
Dividends paid	(168.4)	(145.6)	(154.7)	(165.8)	(176.8)
Equity raised / (purchased)	5.8	(49.1)	0.0	0.0	0.0
Change in Debt	(5.2)	(0.5)	0.0	0.0	0.0
Perpetual securities distribution	0.0	0.0	0.0	0.0	0.0
Other invest/financing cash flow	(87.1)	113.4	27.9	27.1	27.1
Effect of exch rate changes	(3.0)	(4.8)	0.0	0.0	0.0
Net cash flow	(61.6)	94.9	(64.3)	41.6	39.6

FYE 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	(1.8)	(1.9)	0.2	4.4	3.1
EBITDA growth	(13.0)	(0.8)	16.9	5.3	3.1
EBIT growth	(11.1)	4.1	22.9	6.9	4.1
Pretax growth	(4.0)	4.3	22.7	4.9	3.6
Reported net profit growth	(2.4)	8.5	16.1	3.2	3.3
Core net profit growth	(9.4)	7.0	16.0	3.2	3.3
<b>Profitability ratios (%)</b>					
EBITDA margin	13.9	14.0	16.4	16.5	16.5
EBIT margin	9.6	10.2	12.5	12.8	12.9
Pretax profit margin	12.1	12.8	15.7	15.8	15.8
Payout ratio	80.4	79.6	73.0	75.4	77.6
<b>DuPont analysis</b>					
Net profit margin (%)	10.1	11.2	12.9	12.8	12.8
Revenue/Assets (x)	0.9	0.9	0.9	0.9	0.9
Assets/Equity (x)	1.4	1.4	1.3	1.3	1.3
ROAE (%)	13.0	13.7	15.4	15.2	15.0
ROAA (%)	9.1	9.7	11.3	11.4	11.3
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	nm	nm	nm	nm	nm
Days receivable outstanding	59.3	58.5	58.5	57.9	58.3
Days inventory outstanding	231.3	171.6	174.9	257.0	266.3
Days payables outstanding	nm	nm	nm	nm	nm
Dividend cover (x)	1.2	1.3	1.4	1.3	1.3
Current ratio (x)	2.2	2.3	2.9	3.0	3.1
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	4.0	4.0	4.8	4.8	4.9
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	95.0	na	na	na	nm
Debt/EBITDA (x)	0.5	0.4	0.4	0.3	0.3
Capex/revenue (%)	3.2	3.5	4.0	3.8	3.7
Net debt/ (net cash)	(226.6)	(305.6)	(241.3)	(282.9)	(322.5)

Source: Company; Maybank

## Research Offices

### REGIONAL

#### Sadiq CURRIMBHOY

Regional Head, Research & Economics  
(65) 6231 5836 sadiq@maybank-ke.com.sg

#### WONG Chew Hann, CA

Regional Head of Institutional Research  
(603) 2297 8686 wchewh@maybank-ib.com

#### ONG Seng Yeow

Regional Head of Retail Research  
(65) 6231 5839 ongsengyeow@maybank-ke.com.sg

#### TAN Sin Mui

Director of Research  
(65) 6231 5849 sinmui@kimeng.com.hk

### ECONOMICS

#### Suhaimi ILIAS

Chief Economist  
Singapore | Malaysia  
(603) 2297 8682 suhaimi\_ilias@maybank-ib.com

#### Luz LORENZO

Philippines  
(63) 2 849 8836 luz\_lorenzo@maybank-atrke.com

#### Tim LEELAHAPHAN

Thailand  
(66) 2658 6300 ext 1420 tim.l@maybank-ke.co.th

#### JUNIMAN

Chief Economist, BII  
Indonesia  
(62) 21 29228888 ext 29682 juniman@bankbii.com

### STRATEGY

#### Sadiq CURRIMBHOY

Global Strategist  
(65) 6231 5836 sadiq@maybank-ke.com.sg

#### Willie CHAN

Hong Kong / Regional  
(852) 2268 0631 williechan@kimeng.com.hk

### MALAYSIA

#### WONG Chew Hann, CA Head of Research

(603) 2297 8686 wchewh@maybank-ib.com

#### • Strategy

#### Desmond CH'NG, ACA

(603) 2297 8680 desmond.chng@maybank-ib.com

#### • Banking & Finance

#### LIAW Thong Jung

(603) 2297 8688 tjliaw@maybank-ib.com

#### • Oil & Gas Services - Regional

#### ONG Chee Ting, CA

(603) 2297 8678 ct.ong@maybank-ib.com

#### • Plantations - Regional

#### Mohshin AZIZ

(603) 2297 8692 mohshin.aziz@maybank-ib.com

#### • Aviation - Regional • Petrochem

#### YIN Shao Yang, CPA

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

#### • Gaming - Regional • Media

#### 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

#### LEE Yen Ling

(603) 2297 8691 lee.yl@maybank-ib.com

#### • Building Materials • Glove • Ports • Shipping

#### CHAI Li Shin, CFA

(603) 2297 8684 lishin.c@maybank-ib.com

#### • Plantation • Construction & Infrastructure

#### Ivan YAP

(603) 2297 8612 ivan.yap@maybank-ib.com

#### • Automotive • Semiconductor • Technology

#### Kevin WONG

(603) 2082 6824 kevin.wong@maybank-ib.com

#### • REITs • Consumer Discretionary

#### LIEW Wei Han

(603) 2297 8676 weihan.l@maybank-ib.com

#### • Consumer Staples

#### LEE Cheng Hooi Regional Chartist

(603) 2297 8694 chenghooi.lee@maybank-ib.com

#### Tee Sze Chiah Head of Retail Research

(603) 2297 6858 szechiah.t@maybank-ib.com

#### Cheah Chong Ling

(603) 2297 8767 chongling.c@maybank-ib.com

### HONG KONG / CHINA

#### Howard WONG Head of Research

(852) 2268 0648 howardwong@kimeng.com.hk

#### • Oil & Gas - Regional

#### Benjamin HO

(852) 2268 0632 benjaminho@kimeng.com.hk

#### • Consumer & Auto

#### Jacqueline KO, CFA

(852) 2268 0633 jacquelineko@kimeng.com.hk

#### • Consumer Staples & Durables

#### Ka Leong LO, CFA

(852) 2268 0630 kll@kimeng.com.hk

#### • Consumer Discretionary & Auto

#### Mitchell KIM

(852) 2268 0634 mitchellkim@kimeng.com.hk

#### • Internet & Telcos

#### Osbert TANG, CFA

(86) 21 5096 8370 osberttang@kimeng.com.hk

#### • Transport & Industrials

#### Stefan CHANG, CFA

(852) 2268 0675 stefanchang@kimeng.com.hk

#### • Technology

#### Steven ST CHAN

(852) 2268 0645 stevenchan@kimeng.com.hk

#### • Banking & Financials - Regional

#### Warren LAU

(852) 2268 0644 warrenlau@kimeng.com.hk

#### • Technology - Regional

### INDIA

#### Jigar SHAH Head of Research

(91) 22 6623 2632 jigar@maybank-ke.co.in

#### • Oil & Gas • Automobile • Cement

#### Anubhav GUPTA

(91) 22 6623 2605 anubhav@maybank-ke.co.in

#### • Metal & Mining • Capital Goods • Property

#### Vishal MODI

(91) 22 6623 2607 vishal@maybank-ke.co.in

#### • Banking & Financials

#### Abhijeet KUNDU

(91) 22 6623 2628 abhijeet@maybank-ke.co.in

#### • Consumer

#### Neerav DALAL

(91) 22 6623 2606 neerav@maybank-ke.co.in

#### • Software Technology • Telcos

### SINGAPORE

#### Gregory YAP

(65) 6231 5848 gyap@maybank-ke.com.sg

#### • SMD Caps

#### • Technology & Manufacturing • Telcos

#### YEAK Chee Keong, CFA

(65) 6231 5842 yeakcheekeong@maybank-ke.com.sg

#### • Offshore & Marine

#### Derrick HENG, CFA

(65) 6231 5843 derrickheng@maybank-ke.com.sg

#### • Transport • Property • REITs (Office)

#### Joshua TAN

(65) 6231 5850 joshuat@maybank-ke.com.sg

#### • REITs (Retail, Industrial)

#### John CHEONG

(65) 6231 5845 johncheong@maybank-ke.com.sg

#### • Small & Mid Caps • Healthcare

#### TRUONG Thanh Hang

(65) 6231 5847 hang.truong@maybank-ke.com.sg

#### • Small & Mid Caps

### INDONESIA

#### IsnaputraISKANDAR Head of Research

(62) 21 2557 1129 isnaputra.iskandar@maybank-ke.co.id

#### • Strategy • Metals & Mining • Cement

#### RahmiMARINA

(62) 21 2557 1128 rahmi.marina@maybank-ke.co.id

#### • Banking & Finance

#### AurelliaSETIABUDI

(62) 21 2953 0785 aurellia.setiabudi@maybank-ke.co.id

#### • Property

#### Pandu ANUGRAH

(62) 21 2557 1137 pandu.anugrah@maybank-ke.co.id

#### • Infra • Construction • Transport • Telcos

#### JanniASMAN

(62) 21 2953 0784 janni.asman@maybank-ke.co.id

#### • Cigarette • Healthcare • Retail

#### Adhi TASMIN

(62) 21 2557 1209 adhi.tasmin@maybank-ke.co.id

#### • Plantations

### PHILIPPINES

#### Luz LORENZO Head of Research

(63) 2 849 8836 luz\_lorenzo@maybank-atrke.com

#### • Strategy

#### • Utilities • Conglomerates • Telcos

#### Lovell SARREAL

(63) 2 849 8841 lovell\_sarreal@maybank-atrke.com

#### • Consumer • Media • Cement

#### Rommel RODRIGO

(63) 2 849 8839 rommel\_rodriogo@maybank-atrke.com

#### • Conglomerates • Property • Gaming

#### • Ports/ Logistics

#### Katherine TAN

(63) 2 849 8843 kat\_tan@maybank-atrke.com

#### • Banks • Construction

#### Michael BENGSON

(63) 2 849 8840 michael\_bengson@maybank-atrke.com

#### • Conglomerates

#### Jaclyn JIMENEZ

(63) 2 849 8842 jaclyn\_jimenez@maybank-atrke.com

#### • Consumer

#### Arabelle MAGHIRANG

(63) 2 849 8838 arabelle\_maghirang@maybank-atrke.com

#### • Banks

### THAILAND

#### Maria LAPIZ Head of Institutional Research

Dir (66) 2257 0250 | (66) 2658 6300 ext 1399

Maria.L@maybank-ke.co.th

#### • Consumer • Materials • Ind. Estates

#### SittichaiDUANGRATTANACHAYA

(66) 2658 6300 ext 1393

Sittichai.D@maybank-ke.co.th

#### • Services Sector • Transport

#### SukitUDOMSIRIKUL Head of Retail Research

(66) 2658 6300 ext 5090

Sukit.u@maybank-ke.co.th

#### MayureeCHOWWIKRAN

(66) 2658 6300 ext 1440

mayuree.c@maybank-ke.co.th

#### • Strategy

#### PadonVANNARAT

(66) 2658 6300 ext 1450

Padon.v@maybank-ke.co.th

#### • Strategy

#### Surachai PRAMUALCHAROENKIT

(66) 2658 6300 ext 1470

Surachai.p@maybank-ke.co.th

#### • Auto • Conmat • Contractor • Steel

#### SuttatipPEERASUB

(66) 2658 6300 ext 1430

suttatip.p@maybank-ke.co.th

#### • Media • Commerce

#### SutthichaiKUMWORACHAI

(66) 2658 6300 ext 1400

sutthichai.k@maybank-ke.co.th

#### • Energy • Petrochem

#### TermpornTANTIVIVAT

(66) 2658 6300 ext 1520

termporn.t@maybank-ke.co.th

#### • Property

#### JaroonpanWATTANAWONG

(66) 2658 6300 ext 1404

jaroonpan.w@maybank-ke.co.th

#### • Transportation • Small cap

### VIETNAM

#### LE Hong Lien, ACCA

Head of Institutional Research

(84) 8 44 555 888 x 8181

lien.le@maybank-kimeng.com.vn

#### • Strategy • Consumer • Diversified • Utilities

#### THAI QuangTrung, CFA, Deputy Manager,

Institutional Research

(84) 8 44 555 888 x 8180

thai.truong@maybank-kimeng.com.vn

#### • Real Estate • Construction • Materials

#### Le Nguyen NhatChuyen

(84) 8 44 555 888 x 8082

chuyen.le@maybank-kimeng.com.vn

#### • Oil & Gas

#### NGUYEN ThiNganTuyen, Head of Retail Research

(84) 8 44 555 888 x 8081

tuyen.nguyen@maybank-kimeng.com.vn

#### • Food & Beverage • Oil & Gas • Banking

#### TRINH Thi Ngoc Diep

(84) 8 44 555 888 x 8208

diep.trinh@maybank-kimeng.com.vn

#### • Technology • Utilities • Construction

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**Malaysia**

Maybank Investment Bank Berhad  
(A Participating Organisation of  
Bursa Malaysia Securities Berhad)  
33rd Floor, MenaraMaybank,  
100 JalanTun Perak,  
50050 Kuala Lumpur  
Tel: (603) 2059 1888;  
Fax: (603) 2078 4194

Stockbroking Business:  
Level 8, Tower C, DataranMaybank,  
No.1, JalanMaarof  
59000 Kuala Lumpur  
Tel: (603) 2297 8888  
Fax: (603) 2282 5136


**Philippines**

Maybank ATR Kim Eng Securities Inc.  
17/F, Tower One & Exchange Plaza  
Ayala Triangle, Ayala Avenue  
Makati City, Philippines 1200

Tel: (63) 2 849 8888  
Fax: (63) 2 848 5738


**South Asia Sales Trading**

Kevin Foy  
Regional Head Sales Trading  
kevinfoy@maybank-ke.com.sg  
Tel: (65) 6336-5157  
US Toll Free: 1-866-406-7447

**Malaysia**

Rommel Jacob  
rommeljacob@maybank-ib.com  
Tel: (603) 2717 5152

**Indonesia**

HariantoLiong  
harianto.liong@maybank-ke.co.id  
Tel: (62) 21 2557 1177

**New York**

Andrew Dacey  
adacey@maybank-keusa.com  
Tel: (212) 688 2956

**Vietnam**

Tien Nguyen  
thuytien.nguyen@maybank-kimeng.com.vn  
Tel: (84) 44 555 888 x8079


**Singapore**

Maybank Kim Eng Securities Pte Ltd  
Maybank Kim Eng Research Pte Ltd  
50 North Canal Road  
Singapore 059304

Tel: (65) 6336 9090


**Hong Kong**

Kim Eng Securities (HK) Ltd  
Level 30,  
Three Pacific Place,  
1 Queen's Road East,  
Hong Kong

Tel: (852) 2268 0800  
Fax: (852) 2877 0104


**Thailand**

Maybank Kim Eng Securities  
(Thailand) Public Company Limited  
999/9 The Offices at Central World,  
20<sup>th</sup> - 21<sup>st</sup> Floor,  
Rama 1 Road Pathumwan,  
Bangkok 10330, Thailand

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


**North Asia Sales Trading**

Andrew Lee  
andrewlee@kimeng.com.hk  
Tel: (852) 2268 0283  
US Toll Free: 1 877 837 7635

**Thailand**

TanasakKrishnasreni  
Tanasak.K@maybank-ke.co.th  
Tel:(66)2 658 6820

**India**

Manish Modi  
manish@maybank-ke.co.in  
Tel:(91)-22-6623-2601

**Philippines**

Keith Roy  
keith\_roy@maybank-atrke.com  
Tel:(63) 2 848-5288


**London**

Maybank Kim Eng Securities  
(London) Ltd  
5<sup>th</sup> Floor, Aldermay House  
10-15 Queen Street  
London EC4N 1TX, UK

Tel: (44) 20 7332 0221  
Fax: (44) 20 7332 0302


**Indonesia**

PT Maybank Kim Eng Securities  
Plaza Bapindo  
Citibank Tower 17<sup>th</sup> Floor  
JLJend. SudirmanKav. 54-55  
Jakarta 12190, Indonesia

Tel: (62) 21 2557 1188  
Fax: (62) 21 2557 1189


**Vietnam**

Maybank Kim Eng Securities Limited  
4A-15+16 Floor VincomCenter Dong  
Khoi, 72 Le Thanh Ton St. District 1  
Ho Chi Minh City, Vietnam

Tel : (84) 844 555 888  
Fax : (84) 8 38 271 030


**New York**

Maybank Kim Eng Securities USA  
Inc  
777 Third Avenue, 21st Floor  
New York, NY 10017, U.S.A.

Tel: (212) 688 8886  
Fax: (212) 688 3500


**India**

Kim Eng Securities India Pvt Ltd  
2nd Floor, The International 16,  
Maharishi Karve Road,  
Churchgate Station,  
Mumbai City - 400 020, India

Tel: (91) 22 6623 2600  
Fax: (91) 22 6623 2604


**Saudi Arabia**

*In association with*  
**Anfaal Capital**  
Villa 47, Tujjar Jeddah  
Prince Mohammed bin Abdulaziz  
Street P.O. Box 126575  
Jeddah 21352

Tel: (966) 2 6068686  
Fax: (966) 26068787