

# United Overseas Bank (UOB SP)

## Onwards And Upwards

# BUY

Share Price SGD 28.10  
 12m Price Target SGD 31.08 (+11%)  
 Previous Price Target SGD 29.33

### ROE to recover; EPS and TP raised

We believe UOB can generate robust earnings in a cyclical upturn. We raised FY18-20E net profits by 2-5% mainly on higher loan growth and non-interest income assumptions. With the change in our EPS estimates, our assumed sustainable ROE is now 12.7% (12.1% previously), with COE of 10.1% and a growth rate of 3.5% (both unchanged). Accordingly, our TP is raised 6% to SGD31.08, pegged to ~1.4x FY18E P/BV (from 1.3x), 0.5SD above its historical mean of 1.3x to reflect higher forecast ROEs. Maintain BUY.

### Healthy momentum

We raised FY18-20E loan growth slightly to ~9-10% from 9-9.5% based on an average multiplier between its loan growth and Singapore's GDP growth of 2.6x. A rebound in Singapore's property market can benefit UOB as 50% of its total loan book is related to housing and building and construction (B&C) loan vs 42% for peers. Also, we remain positive on UOB's capability for further WM fee growth. We think UOB's wealth franchise is underappreciated. Its organic AUM grew decently at a 7-year CAGR of 12% (vs peers' 15-22%). FY17 saw solid 12% YoY growth in AUM.

### Scope for higher dividends

With earnings momentum likely to continue, strong fully-loaded CET1 capital at 14.7% and consistent improvement in return on risk-weighted assets in recent quarters, we think there is scope for capital management and higher dividends. We raised our FY18-20E DPS forecast to SGD1.20-1.40/sh (from SGD1/sh). This implies payout ratio of 42-46%.

### Maintain BUY

We like UOB's disciplined pricing strategy and its sensitivity to re-pricing intervals. Risks to our BUY thesis are: 1) lower income; and 2) higher provisions.

FYE Dec (SGD m)	FY16A	FY17A	FY18E	FY19E	FY20E
Operating income	8,061	8,851	10,037	11,107	12,325
Pre-provision profit	4,365	4,824	5,734	6,532	7,458
Core net profit	3,004	3,299	4,259	4,821	5,482
Core EPS (SGD)	1.8	2.0	2.6	2.9	3.4
Core EPS growth (%)	(5.2)	9.8	29.1	13.2	13.7
Net DPS (SGD)	0.7	1.0	1.2	1.3	1.4
Core P/E (x)	15.3	13.9	10.8	9.5	8.4
P/BV (x)	1.5	1.3	1.2	1.2	1.1
Net dividend yield (%)	2.5	3.6	4.3	4.6	5.0
Book value (SGD)	18.77	21.20	22.49	24.08	25.97
ROAE (%)	10.1	10.1	11.9	12.7	13.4
ROAA (%)	0.9	0.9	1.1	1.2	1.3
Consensus net profit	-	-	3,856	4,300	4,623
MKE vs. Consensus (%)	-	-	12.9	14.3	20.6

Ng Li Hiang  
 nglihiang@maybank-ke.com.sg  
 (65) 6231 5840

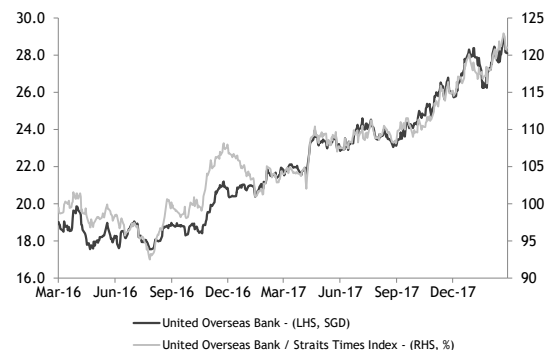
### Statistics

52w high/low (SGD)	28.99/21.47
3m avg turnover (USDm)	54.1
Free float (%)	77.5
Issued shares (m)	1,615
Market capitalisation	SGD45.4B
	USD34.4B

### Major shareholders:

WEE FAMILY	18.1%
LIEN FAMILY	5.2%

### Price Performance



	-1M	-3M	-12M
Absolute (%)	3	8	28
Relative to index (%)	2	5	16

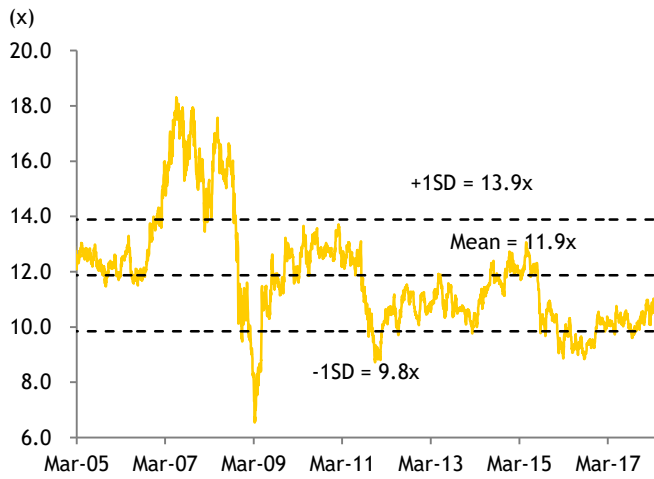
Source: FactSet

**Fig 1: Revisions to estimates**

UOB	Revised			Original		
	2018E	2019E	2020E	2018E	2019E	2020E
<b>(SGD m)</b>						
Net interest income	6,321.8	6,978.6	7,728.7	6,290.2	6,915.2	7,631.4
Non-interest income	3,715.6	4,128.0	4,596.5	3,644.0	3,979.6	4,340.4
Total income	10,037.4	11,106.6	12,325.2	9,934.2	10,894.9	11,971.8
Expenses	(4,303.1)	(4,574.5)	(4,867.5)	(4,303.1)	(4,574.5)	(4,867.5)
Provisions	(522.2)	(639.3)	(764.5)	(516.4)	(627.3)	(742.3)
Net profit <sup>^</sup>	4,259.4	4,821.4	5,481.9	4,179.5	4,657.6	5,210.3
<b>Revisions (%)</b>						
Net interest income	0.5	0.9	1.3			
Non-interest income	2.0	3.7	5.9			
Total income	1.0	1.9	3.0			
Expenses	-	-	-			
Provisions	1.1	1.9	3.0			
Net profit <sup>^</sup>	1.9	3.5	5.2			

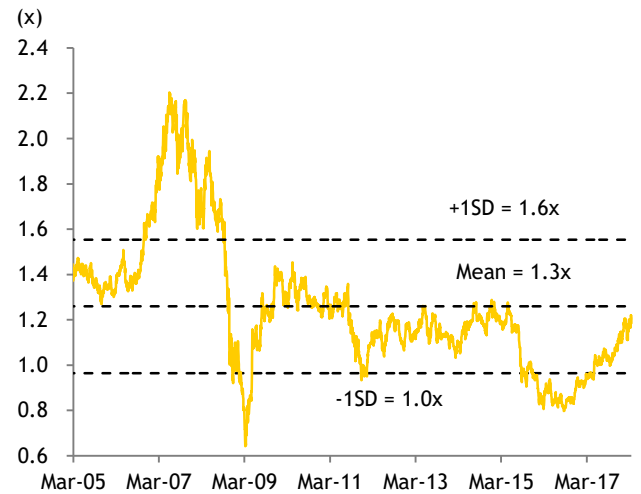
Source: Maybank Kim Eng. <sup>^</sup>Net profit excludes one-offs and preference share dividends

**Fig 2: UOB's 12M forward rolling PER band**



Source: Bloomberg, Maybank Kim Eng

**Fig 3: UOB's 12M forward rolling P/BV band**

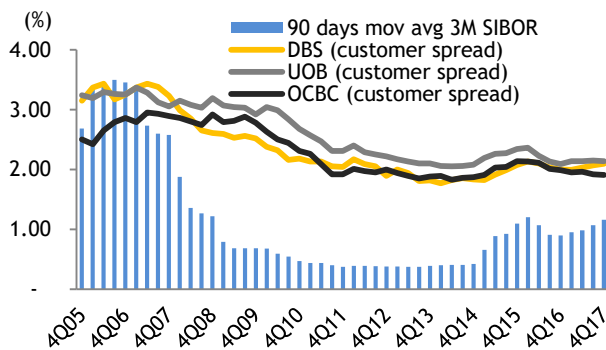


Source: Bloomberg, Maybank Kim Eng

## Value Proposition

- Largest SME lender, reflecting its Chinese roots and legacy relationships, resulting in higher lending yields than peers.
- Corporate culture empowers branch managers to support SMEs in the heartlands, cultivating and fortifying relationships - a differentiating factor.
- Conservative, focused on traditional banking. Headed by founding family, which is not inclined to make aggressive overseas or treasury bets. Works well for harsh landscape.
- Strengthening regional footprint - Indonesia, Thailand, Malaysia and Hong Kong. Focus on Indonesia and consumer.
- But Goldilocks era (2010-2014) of low credit costs and asset expansion may be over.

### UOB's customer spreads at 2.14% in 4Q17

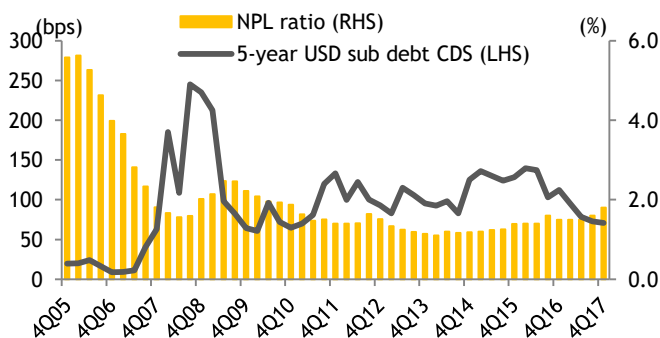


Source: Bloomberg, Companies.

## Financial Metrics

- Asset quality: 1.8% NPL ratio in FY17. Higher NPL ratio seen in transport sector at 12.9% and Indonesia at 6.5%.
- Fully-loaded CET1 was 14.7% as at 4Q17, above management's comfort level of 12.5%. See scope for capital management and dividend upside.
- Expect -9-10% net loan growth in FY18-20E.
- Expect FY18/19/20E NIMs at 1.83%/1.87%/1.92%.
- Cost of capital will be a major consideration for the sector. Contagion risks, which may be reflected in its corporate papers or CDS, ought to be carefully watched.

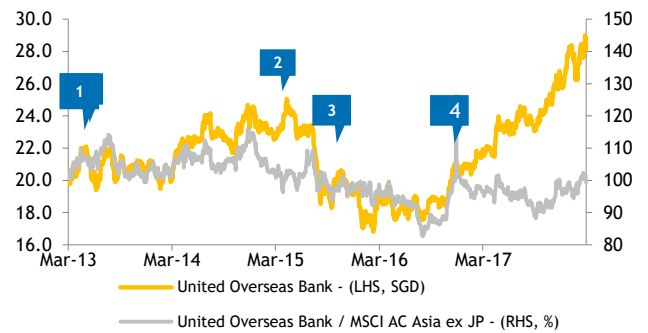
### NPL ratio followed CDS spreads with a lag



Source: Bloomberg, Company

## Price Drivers

### Historical share price



Source: FactSet, Maybank Kim Eng

1. +20% broad-based rebound in 2012 core PATMI.
2. Record earnings with robust lending and asset resilience.
3. Weaker-than-expected 2H15, sharp CNY devaluation in August and O&G/commodity NPL worries.
4. Share price rallied on positive sentiment from interest rate hikes, USD strength and economic recovery. Risks from O&G abated.

## Swing Factors

### Upside

- Sharp and sustained rebound in commodity prices ease concerns about global risks.
- Ability to re-price assets at higher interest rates, widening credit spreads.
- Proactive restructuring of loans allows asset quality to hold up better than expected, with no major credit slippages.
- Higher demand for domestic mortgages from easing of property-cooling measures.

### Downside

- Asset-quality deterioration becomes a systemic problem, especially if job losses in Singapore become pervasive and hurt the mortgage portfolio.
- Shocks in the fixed-income portfolio.
- Lack of liquidity of a funding currency.
- Succession issues.
- Major changes in the competitive banking landscape in Singapore that result in the emergence of a dominant financial institution.
- Translational losses from MYR/IDR depreciation.
- Capital raising by any institution in sector.

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
<b>Key Metrics</b>					
Core P/E (x)	15.3	13.9	10.8	9.5	8.4
Core FD P/E (x)	15.3	13.9	10.8	9.5	8.4
P/BV (x)	1.5	1.3	1.2	1.2	1.1
P/NTA (x)	1.7	1.5	1.4	1.3	1.2
Net dividend yield (%)	2.5	3.6	4.3	4.6	5.0

**INCOME STATEMENT (SGD m)**

Interest income	8,290.5	9,077.0	10,367.6	11,569.1	12,967.2
Interest expense	(3,299.8)	(3,548.0)	(4,045.8)	(4,590.4)	(5,238.5)
<b>Net interest income</b>	<b>4,990.8</b>	<b>5,529.0</b>	<b>6,321.8</b>	<b>6,978.6</b>	<b>7,728.7</b>
Net insurance income	0.0	0.0	0.0	0.0	0.0
Net fees and commission	1,930.6	2,161.0	2,457.5	2,759.2	3,091.7
Other income	1,139.9	1,161.0	1,258.1	1,368.8	1,504.8
<b>Total non-interest income</b>	<b>3,070.5</b>	<b>3,322.0</b>	<b>3,715.6</b>	<b>4,128.0</b>	<b>4,596.5</b>
<b>Operating income</b>	<b>8,061.3</b>	<b>8,851.0</b>	<b>10,037.4</b>	<b>11,106.6</b>	<b>12,325.2</b>
Staff costs	(2,050.0)	(2,224.0)	(2,344.4)	(2,462.1)	(2,586.0)
Other operating expenses	(1,646.5)	(1,803.0)	(1,958.8)	(2,112.4)	(2,281.5)
<b>Operating expenses</b>	<b>(3,696.5)</b>	<b>(4,027.0)</b>	<b>(4,303.1)</b>	<b>(4,574.5)</b>	<b>(4,867.5)</b>
<b>Pre-provision profit</b>	<b>4,364.8</b>	<b>4,824.0</b>	<b>5,734.3</b>	<b>6,532.1</b>	<b>7,457.7</b>
Loan impairment allowances	(593.8)	(727.0)	(522.2)	(639.3)	(764.5)
Other allowances	0.0	0.0	0.0	0.0	0.0
Associates & JV income	5.9	110.0	115.5	121.3	127.3
<b>Pretax profit</b>	<b>3,776.9</b>	<b>4,207.0</b>	<b>5,327.6</b>	<b>6,014.0</b>	<b>6,820.6</b>
Income tax	(669.0)	(800.0)	(959.0)	(1,082.5)	(1,227.7)
Minorities	(11.7)	(16.0)	(16.8)	(17.6)	(18.5)
Discontinued operations	0.0	0.0	0.0	0.0	0.0
<b>Reported net profit</b>	<b>3,096.3</b>	<b>3,391.0</b>	<b>4,351.8</b>	<b>4,913.9</b>	<b>5,574.3</b>
<b>Core net profit</b>	<b>3,003.9</b>	<b>3,298.6</b>	<b>4,259.4</b>	<b>4,821.4</b>	<b>5,481.9</b>
Preferred Dividends	92.4	92.4	92.4	92.4	92.4

**BALANCE SHEET (SGD m)**

Cash & deposits with banks	40,032.9	52,181.0	53,746.4	55,358.8	57,019.6
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	6,981.5	5,292.8	5,398.7	5,506.7	5,616.8
Dealing securities	5,489.8	4,276.6	4,866.7	5,048.6	5,237.8
Available-for-sale securities	8,462.6	9,314.2	9,314.2	9,314.2	9,314.2
Investment securities	18,330.0	15,424.2	15,970.0	16,536.3	17,123.9
Loans & advances	221,733.7	232,212.0	254,899.1	278,974.3	306,550.9
Central bank deposits	24,322.1	26,625.0	28,916.1	31,388.4	34,175.7
Investment in associates/JVs	1,108.9	1,194.0	1,205.9	1,218.0	1,230.2
Insurance assets	0.0	0.0	0.0	0.0	0.0
Fixed assets	2,989.8	3,059.0	3,104.9	3,151.5	3,198.7
Intangible assets	4,151.0	4,142.0	4,142.0	4,142.0	4,142.0
Other assets	6,425.3	4,871.2	4,631.5	4,554.6	4,458.5
<b>Total assets</b>	<b>340,027.6</b>	<b>358,592.0</b>	<b>386,195.5</b>	<b>415,193.3</b>	<b>448,068.3</b>
Deposits from customers	255,314.0	272,765.0	296,236.4	321,564.6	350,119.6
Deposits from banks & FIs	11,855.2	11,440.0	11,726.0	12,136.4	12,682.5
Derivatives financial instruments	6,837.1	5,962.2	6,051.6	6,142.4	6,234.5
Subordinated debt	5,926.0	4,827.0	4,827.0	4,827.0	4,827.0
Other securities in issue	16,541.0	16,674.9	17,109.9	17,557.8	18,019.2
Other borrowings	5,853.6	5,853.6	5,853.6	5,853.6	5,853.6
Insurance liabilities	0.0	0.0	0.0	0.0	0.0
Other liabilities	6,836.7	6,208.8	7,421.3	7,537.4	7,656.4
<b>Total liabilities</b>	<b>309,163.5</b>	<b>323,731.5</b>	<b>349,225.8</b>	<b>375,619.2</b>	<b>405,392.9</b>
Share capital	1,635.7	1,662.7	1,662.7	1,662.7	1,662.7
Reserves	29,060.0	33,009.8	35,118.4	37,721.0	40,820.5
Shareholders' funds	30,695.6	34,672.5	36,781.0	39,383.6	42,483.1
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	168.6	187.0	188.7	190.4	192.3
Total equity	30,864.2	34,859.5	36,969.7	39,574.1	42,675.4
<b>Total liabilities &amp; equity</b>	<b>340,027.6</b>	<b>358,592.0</b>	<b>386,195.5</b>	<b>415,193.3</b>	<b>448,068.3</b>

FYE 31 Dec	FY16A	FY17A	FY18E	FY19E	FY20E
<b>Key Ratios</b>					
<b>Growth (%)</b>					
Net interest income	1.3	10.8	14.3	10.4	10.7
Non-interest income	(1.6)	8.2	11.8	11.1	11.3
Operating expenses	2.8	8.9	6.9	6.3	6.4
Pre-provision profit	(1.9)	10.5	18.9	13.9	14.2
Core net profit	(3.2)	9.8	29.1	13.2	13.7
Gross loans	8.8	4.7	9.7	9.4	9.9
Customer deposits	6.1	6.8	8.6	8.5	8.9
Total assets	7.6	5.5	7.7	7.5	7.9
<b>Profitability (%)</b>					
Non-int. income/Total income	38.1	37.5	37.0	37.2	37.3
Average lending yields	2.84	2.91	3.00	3.10	3.21
Average cost of funds	1.16	1.18	1.26	1.32	1.40
Net interest margin	1.71	1.77	1.83	1.87	1.92
Cost/income	45.9	45.5	42.9	41.2	39.5
<b>Liquidity (%)</b>					
Loans/customer deposits	86.8	85.1	86.0	86.8	87.6
<b>Asset quality (%)</b>					
Net NPL	1.5	1.8	1.4	1.5	1.6
Gross NPL	1.5	1.8	1.4	1.5	1.6
(SP+GP)/average gross loans	0.3	0.3	0.2	0.2	0.3
Loan loss coverage	116.3	90.9	112.4	104.2	98.4
<b>Capital adequacy (%)</b>					
CET1	13.1	16.2	16.2	16.5	16.6
Tier 1 capital	13.1	16.2	16.2	16.5	16.6
Risk-weighted capital	16.2	18.7	18.4	18.5	18.5
<b>Returns (%)</b>					
ROAE	10.1	10.1	11.9	12.7	13.4
ROAA	0.9	0.9	1.1	1.2	1.3
Shareholders equity/assets	9.0	9.7	9.5	9.5	9.5

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  
Malaysia | Philippines | China  
(603) 2297 8682  
suhaimi\_ilias@maybank-ib.com

**CHUA Hak Bin**  
Regional Thematic Macroeconomist  
(65) 6231 5830  
chuahb@maybank-ke.com.sg

**LEE Ju Ye**  
Singapore  
(65) 6231 5844  
leejuye@maybank-ke.com.sg

**Dr Zamros DZULKAFLI**  
(603) 2297 8618  
zamros.d@maybank-ib.com

**Ramesh LANKANATHAN**  
(603) 2297 8685  
ramesh@maybank-ib.com

### FX

**Saktiandi SUPAAT**  
Head, FX Research  
(65) 6231 1379  
saktiandi@maybank.com.sg

**Christopher WONG**  
(65) 6320 1347  
wongkl@maybank.com.sg

**Leslie TANG**  
(65) 6320 1378  
leslietang@maybank.com.sg

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

### 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

### FIXED INCOME

**Winson Phoon, ACA**  
(65) 6231 5831  
winsonphoon@maybank-ke.com.sg

**Se Tho Mun Yi**  
(603) 2074 7606  
munyi.st@maybank-ib.com

### 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

**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

**Adrian WONG**  
(603) 2297 8675 adrian.wkj@maybank-ib.com  
• Constructions • Healthcare

**Jade TAM**  
(603) 2297 8687 jade.tam@maybank-ib.com  
• Media • Building Materials

**Mohd Hafiz Hassan**  
(603) 2082 6819 mohdhafiz.ha@maybank-ib.com  
• Small & Mid Caps

**TEE Sze Chiah** *Head of Retail Research*  
(603) 2082 6858 szechiah.t@maybank-ib.com

**Nik Ihsan Raja Abdullah, MSTA, CFTe**  
(603) 2297 8694  
nikmohdihsan.ra@maybank-ib.com

### SINGAPORE

**Neel SINHA** *Head of Research*  
(65) 6231 5838 neelsinha@maybank-ke.com.sg  
• Strategy  
• SMID Caps - Regional

**CHUA Su Tye**  
(65) 6231 5842 chuasutye@maybank-ke.com.sg  
• REITs

**Derrick HENG, CFA**  
(65) 6231 5843 derrickheng@maybank-ke.com.sg  
• Property • REITs (Office)

**Luis HILADO**  
(65) 6231 5848 luishilado@maybank-ke.com.sg  
• Telcos

**John CHEONG, CFA**  
(65) 6231 5845 johncheong@maybank-ke.com.sg  
• Small & Mid Caps • Healthcare • Transport

**NG Li Hiang**  
(65) 6231 5840 nglhiang@maybank-ke.com.sg  
• Banks

**LAI Gene Lih**  
(65) 6231 5832 laigenetih@maybank-ke.com.sg  
• Technology

### HONG KONG / CHINA

**Christopher WONG**  
(852) 2268 0652  
christopherwong@kimeng.com.hk  
• HK & China Properties

**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

**Ricky NG, CFA**  
(852) 2268 0689 rickyng@kimeng.com.hk  
• Regional Renewables  
• HK & China Properties

**Sonija LI, CFA, FRM**  
(852) 2268 0641 sonijali@kimeng.com.hk  
• Gaming

**Stefan CHANG, CFA**  
(852) 2268 0675 stefanchang@kimeng.com.hk  
• Technology - Regional

**Bonny WENG**  
(852) 2268 0644 bonnyweng@kimeng.com.hk  
• Technology - Regional

**Tony REN, CFA**  
(852) 2268 0640 tonyren@kimeng.com.hk  
• Healthcare & Pharmaceutical

### INDIA

**Jigar SHAH** *Head of Research*  
(91) 22 6623 2632 jigar@maybank-ke.co.in  
• Strategy • Oil & Gas • Automobile • Cement

**Vishal MODI**  
(91) 22 6623 2607 vishal@maybank-ke.co.in  
• Banking & Financials

**Neerav DALAL**  
(91) 22 6623 2606 neerav@maybank-ke.co.in  
• Software Technology • Telcos

**Vishal PERIWAL**  
(91) 22 6623 2605 vishalperiwa@maybank-ke.co.in  
• Infrastructure

### INDONESIA

**Isnaputra ISKANDAR** *Head of Research*  
(62) 21 8066 8680  
isnaputra.iskandar@maybank-ke.co.id  
• Strategy • Metals & Mining • Cement

**Rahmi MARINA**  
(62) 21 8066 8689  
rahmi.marina@maybank-ke.co.id  
• Banking & Finance

**Aurellia SETIABUDI**  
(62) 21 8066 8691  
aurellia.setiabudi@maybank-ke.co.id  
• Property

**Janni ASMAN**  
(62) 21 8066 8687  
janni.asman@maybank-ke.co.id  
• Cigarette • Healthcare • Retail

### PHILIPPINES

**Minda OLONAN** *Head of Research*  
(63) 2 849 8840  
minda\_olonan@maybank-atrke.com  
• Strategy

**Katherine TAN**  
(63) 2 849 8843  
kat\_tan@maybank-atrke.com  
• Banks • Construction

**Luis HILADO**  
(65) 6231 5848 luishilado@maybank-ke.com.sg  
• Telcos

### THAILAND

**Maria LAPIZ** *Head of Institutional Research*  
Dir (66) 2257 0250 | (66) 2658 6300 ext 1399  
Maria.L@maybank-ke.co.th  
• Strategy • Consumer • Materials • Ind. Estates  
• Oil & Gas • Telcos

**Sittichai DUANGRATTANACHAYA**  
(66) 2658 6300 ext 1393  
Sittichai.D@maybank-ke.co.th  
• Services Sector • Transport • Property • Telcos

**Tanawat RUENBANTERNG**  
(66) 2658 6300 ext 1394  
Tanawat.R@maybank-ke.co.th  
• Banks & Diversified Financials

**Ornmongkol TANTITANATORN**  
(66) 2658 6300 ext 1395  
ormmongkol.t@maybank-ke.co.th  
• Oil & Gas

**Sukit UDOMSIRIKUL** *Head of Retail Research*  
(66) 2658 5000 ext 5090  
Sukit.u@maybank-ke.co.th

**Ekachai TARAPORNITIP** *Deputy Head*  
(66) 2658 5000 ext 1530  
Ekachai.t@maybank-ke.co.th

**Surachai PRAMUALCHAROENKIT**  
(66) 2658 5000 ext 1470  
Surachai.p@maybank-ke.co.th  
• Auto • Conmat • Contractor • Steel

**Suttatip PEERASUB**  
(66) 2658 5000 ext 1430  
suttatip.p@maybank-ke.co.th  
• Media • Commerce

**Sutthichai KUMWORACHAI**  
(66) 2658 5000 ext 1400  
sutthichai.k@maybank-ke.co.th  
• Energy • Petrochem

**Termporn TANTIVIVAT**  
(66) 2658 5000 ext 1520  
termporn.t@maybank-ke.co.th  
• Property

**Jaroopan WATTANAWONG**  
(66) 2658 5000 ext 1404  
jaroopan.w@maybank-ke.co.th  
• Transportation • Small cap

**Sorabhol VIRAMTEEKUL** *Head of Digital Research*  
(66) 2658 5000 ext 1550  
sorabhol.v@maybank-ke.co.th  
• Food, Transportation

**Wijit ARAYAPISIT**  
(66) 2658 5000 ext 1450  
wijit.a@maybank-ke.co.th  
• Strategist

### VIETNAM

**LE Hong Lien, ACCA**  
*Head of Institutional Research*  
(84 28) 44 555 888 x 8181  
lien.le@maybank-kimeng.com.vn  
• Strategy • Consumer • Diversified

**THAI Quang Trung, CFA,**  
*Deputy Head, Institutional Research*  
(84 28) 44 555 888 x 8180  
trung.thai@maybank-kimeng.com.vn  
• Real Estate • Construction • Materials

**LE Nguyen Nhat Chuyen**  
(84 28) 44 555 888 x 8082  
chuyen.le@maybank-kimeng.com.vn  
• Oil & Gas

**NGUYEN Thi Ngan Tuyen,**  
*Head of Retail Research*  
(84 28) 44 555 888 x 8081  
tuyen.nguyen@maybank-kimeng.com.vn  
• Food & Beverage • Oil & Gas • Banking

**TRUONG Quang Binh,**  
*Deputy Head, Retail Research*  
(84 28) 44 555 888 x 8087  
binh.truong@maybank-kimeng.com.vn  
• Rubber Plantation • Tyres & Tubes • Oil & Gas

**TRINH Thi Ngoc Diep**  
(84 28) 44 555 888 x 8208  
diep.trinh@maybank-kimeng.com.vn  
• Technology • Utilities • Construction

**NGUYEN Thi Sony Tra Mi**  
(84 28) 44 555 888 x 8084  
mi.nguyen@maybank-kimeng.com.vn  
• Port Operation • Pharmaceutical  
• Food & Beverage

**NGUYEN Thanh Lam**  
(84 28) 44 555 888 x 8086  
thanhlam.nguyen@maybank-kimeng.com.vn  
• Technical Analysis

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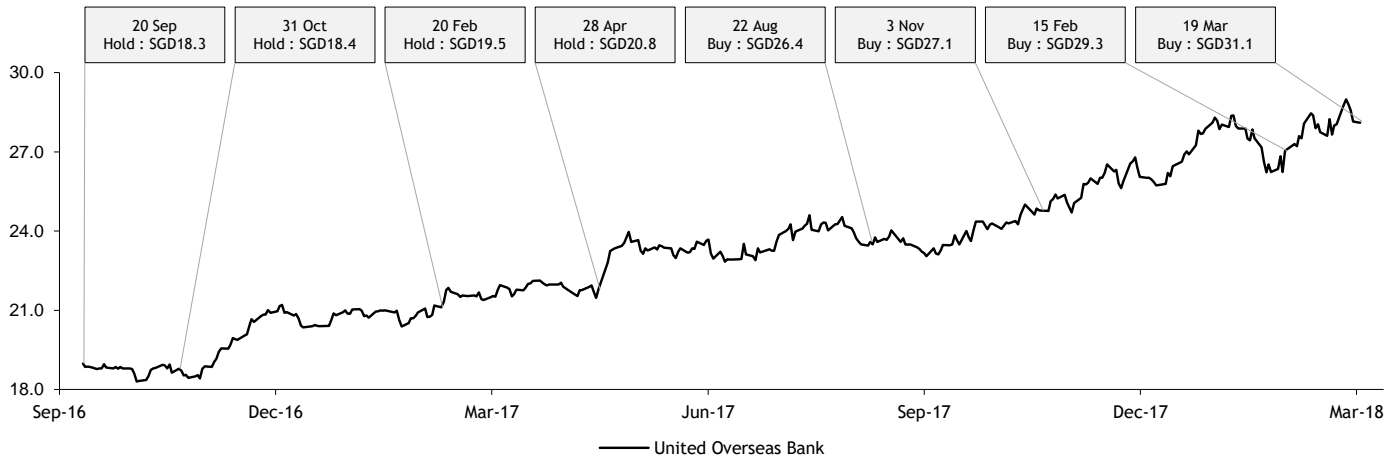
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**Malaysia**

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


**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) 6636-3620  
US Toll Free: 1-866-406-7447

**Malaysia**

Joann Lim  
joann.lim@maybank-ib.com  
Tel: (603) 2717 5166

**Indonesia**

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

**New York**

James Lynch  
jlynch@maybank-keusa.com  
Tel: (212) 688 8886

**Vietnam**

Patrick Mitchell  
patrick.mitchell@maybank-kimeng.com.vn  
Tel: (84)-8-44-555-888 x8080


**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  
28/F, Lee Garden Three,  
1 Sunning Road, Causeway Bay,  
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**

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

**London**

Mark Howe  
mhowe@maybank-ke.co.uk  
Tel: (44) 207-332-0221

**India**

Sanjay Makhija  
sanjaymakhija@maybank-ke.co.in  
Tel: (91)-22-6623-2629

**Philippines**

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


**London**

Maybank Kim Eng Securities  
(London) Ltd  
PNB House  
77 Queen Victoria Street  
London EC4V 4AY, UK

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


**Indonesia**

PT Maybank Kim Eng Securities  
Sentral Senayan III, 22<sup>nd</sup> Floor  
Jl. Asia Afrika No. 8  
Gelora Bung Karno, Senayan  
Jakarta 10270, Indonesia

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


**Vietnam**

Maybank Kim Eng Securities Limited  
4A-15+16 Floor Vincom Center 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