Maybank IB Research

REITs

Malaysia

MRCB-Quill REIT (MQREIT MK)

Positive 2Q16

BUY *[Prior:HOLD]*

Share Price	MYR 1.20
12m Price Target	MYR 1.23 (+3%)
Previous Price Target	*MYR 1.10*

Upgrade to BUY

2Q16 results was a positive surprise whereby the higher net profit margin was lifted by higher revenue, lower opex and lower net financing costs. The 1st interim gross DPU of 4.23sen was also better than expected. We adjust FY16-18 net profit forecasts by +4-6% and raise our DCF-TP by 13sen to MYR1.23 after revising our valuation parameters. Long-term lease agreements provide for resilient earnings while dividend yields at 6.4% net are attractive, these being the premise of our revised BUY call.

Profit margin has improved

2Q16 net profit was MYR15.4m (+12.9% YoY, +1.0% QoQ), bringing 1H16 net profit to MYR30.6m (+39.8% YoY) which accounted for 54%/53% of our/consensus' FY16 estimates. YoY, 2Q16 earnings were lifted by: 1) higher revenue (+1.2%, +MYR0.4m) from step-up rent adjustments at QB2, QB3, QB8, 2) lower operating expenses (-12.7%, -MYR1.0m) namely from Platinum Sentral and Plaza Mont Kiara, and 3) lower financing expenses (-2.6%, -MYR0.4m) attributed to lower total borrowings and higher amount of cash placed in financial institutions. Hence, 2Q16 net profit margin improved to 47.2% from 42.4% in 2Q15. Meanwhile, QoQ earnings were flattish as rental income across its portfolio was stable.

Raising forecasts

We raise FY16/17/18 net profit forecasts by 5.5%/4.2%/4.1% after incorporating lower opex assumptions at Platinum Sentral. We also raise our DCF-based TP by 13sen to MYR1.23 (WACC: 6.6%, terminal yield: 7%) as we roll forward our valuation base year to FY17 and peg our WACC to a lower beta of 0.55x (from 0.60x) which reflects lower risks. MQREIT has successfully renewed 87% of its leases due for renewal in 1H16 and is in advanced talks for the balance of leases up for renewal in 2016. Average occupancy rate remains resilient at 97.2% of NLA at end-Jun 2016.

Earnings to remain resilient

We remain positive on MQREIT's office assets with tenants on long-term leases such as Platinum Sentral (40% of FY16E revenue) and the upcoming Menara Shell which has two anchor tenants on 15-year leases. Menara Shell is estimated to lift our FY17-18 earnings forecasts for MQREIT by ~44% and the acquisition is expected to be completed in 4Q16.

FYE Dec (MYR m)	FY14A	FY15A	FY16E	FY17E	FY18E
Revenue	70	115	126	188	194
Net property income	53	90	104	149	154
Core net profit	34	54	60	92	96
Core EPU (sen)	8.8	8.2	9.1	8.6	9.0
Core EPU growth (%)	(1.1)	(6.7)	11.1	(5.5)	5.3
Net DPU (sen)	7.5	6.9	7.7	7.7	8.1
Net DPU growth (%)	0.0	(8.1)	10.8	0.5	5.3
P/NAV (x)	0.9	0.9	0.9	0.9	0.9
Net DPU yield (%)	6.3	5.8	6.4	6.4	6.8
ROAE (%)	6.4	7.5	6.6	8.1	7.1
ROAA (%)	4.0	4.3	3.7	4.6	4.1
Debt/Assets (x)	0.35	0.42	0.42	0.39	0.39
Consensus Net DPU	-	-	7.4	7.2	7.6
MKE vs. Consensus (%)	-	-	4.1	6.6	6.4

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

Company Description

MRCB-Quill REIT engages in the investment in commercial properties which are mainly located in the Klang Valley.

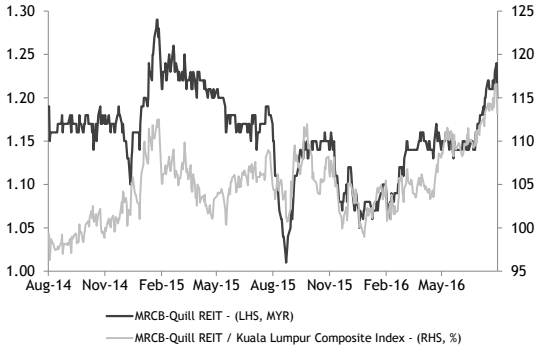
Statistics

52w high/low (MYR)	1.24/1.01
3m avg turnover (USDm)	0.1
Free float (%)	27.6
Issued shares (m)	661
Market capitalisation	MYR793.7M
	USD197M

Major shareholders:

Malaysian Resources Corp. Bhd.	31.2%
CapitaLand Commercial Trust	17.7%
Quill Land Sdn. Bhd.	7.4%

Price Performance



	-1M	-3M	-12M
Absolute (%)	3	3	2
Relative to index (%)	2	4	6

Source: FactSet

Fig 1: Results summary table

	Quarterly					Cumulative		
FY Dec (MYR m)	**2QFY16**	**2QFY15**	***%YoY***	**1QFY16**	***%QoQ***	**1HFY16**	**1HFY15**	***%YoY***
Gross revenue	32.6	32.2	*1.2*	32.7	*(0.3)*	65.2	50.8	*28.4*
Net property income	**25.7**	**24.3**	***5.7***	**25.4**	***1.0***	**51.1**	**38.0**	***34.6***
Interest income	0.4	0.1	*>100*	0.4	*(2.4)*	0.8	0.3	*186.2*
Fair value gains	-	-	*n.m.*	-	*n.m.*	-	-	*n.m.*
Finance costs	(8.0)	(8.2)	*(2.6)*	(7.9)	*1.5*	(15.8)	(11.7)	*35.0*
Other expenses	(2.7)	(2.6)	*3.1*	(2.7)	*(1.0)*	(5.5)	(4.6)	*18.1*
Pretax profit	**15.4**	**13.6**	***12.9***	**15.2**	***1.0***	**30.6**	**21.9**	***39.8***
Tax	-	-	*n.m.*	-	*n.m.*	-	-	*n.m.*
Net profit	**15.4**	**13.6**	***12.9***	**15.2**	***1.0***	**30.6**	**21.9**	***39.8***
Net profit ex-EI	**15.4**	**13.6**	***12.9***	**15.2**	***1.0***	**30.6**	**21.9**	***39.8***
EPU ex-EI (sen) *	2.3	2.2	*5.9*	2.3	*1.3*	4.6	4.3	*7.9*
Gross DPU (sen) ^	**4.2**	**2.2**	***90.5***	**-**	***n.m.***	**4.2**	**3.3**	***27.1***
	2QFY16	**2QFY15**	***+/- ppt***	**1QFY16**	***+/- ppt***	**1HFY16**	**1HFY15**	***+/- ppt***
Net property margin (%)	78.9	75.6	*3.4*	77.9	*1.0*	78.4	74.8	*3.6*
Net income ex-EI margin (%)	47.2	42.4	*4.9*	46.7	*0.6*	47.0	43.1	*3.8*

** Based on reported figures*

^ 1HFY15 includes first interim gross DPU of 1.11sen (declared prior to issuance of new units in 1Q15) which has been adjusted based on 690.1m units (pre-adjustment: 1.88sen)

Sources: Trust, Maybank Kim Eng

FYE 31 Dec	FY14A	FY15A	FY16E	FY17E	FY18E
Key Metrics					
Price/DPU(x)	15.9	17.3	15.6	15.6	14.8
P/BV (x)	0.9	0.9	0.9	0.9	0.9
P/NTA (x)	0.9	0.9	0.9	0.9	0.9
DPU yield (%)	7.0	6.4	7.1	7.1	7.5
FCF yield (%)	8.6	8.9	10.8	7.4	8.9
INCOME STATEMENT (MYR m)					
Revenue	70.2	115.2	125.8	187.6	193.6
Net property income	**53.3**	**90.3**	**103.7**	**149.2**	**154.1**
Management and trustee fees	(5.8)	(9.8)	(13.1)	(19.1)	(19.4)
Net financing costs	(13.3)	(26.5)	(30.6)	(38.6)	(38.3)
Associates & JV	0.0	0.0	0.0	0.0	0.0
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	**34.2**	**54.0**	**60.0**	**91.5**	**96.3**
Income tax	0.0	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0	0.0
Discontinued operations	0.0	0.0	0.0	0.0	0.0
Net profit	**34.2**	**54.0**	**60.0**	**91.5**	**96.3**
Distributable inc to unitholders	34.2	54.0	60.0	91.5	96.3
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	23.3	44.9	73.9	83.4	91.0
Accounts receivable	6.1	5.7	5.7	5.7	5.7
Property, Plant & Equip (net)	0.0	0.0	0.0	0.0	0.0
Inverstment properties	837.7	1,569.8	1,574.8	2,224.8	2,234.8
Intangible assets	0.0	0.0	0.0	0.0	0.0
Investment in Associates & JVs	0.0	0.0	0.0	0.0	0.0
Other assets	1.2	4.9	0.0	0.0	0.0
Total assets	**868.4**	**1,625.3**	**1,654.4**	**2,313.9**	**2,331.5**
ST interest bearing debt	0.0	0.0	0.0	0.0	0.0
Accounts payable	12.2	13.6	13.6	13.6	13.6
LT interest bearing debt	305.1	689.7	689.7	898.4	898.4
Other liabilities	9.8	18.1	43.5	46.3	63.9
Total Liabilities	**327.1**	**721.5**	**746.9**	**958.3**	**975.9**
Shareholders Equity	541.3	903.9	907.5	1,355.6	1,355.6
Minority Interest	0.0	0.0	0.0	0.0	0.0
Total shareholder equity	**541.3**	**903.9**	**907.5**	**1,355.6**	**1,355.6**
Total liabilities and equity	**868.4**	**1,625.3**	**1,654.4**	**2,313.9**	**2,331.5**
CASH FLOW (MYR m)					
Cash flow from operations	**40.1**	**70.6**	**85.5**	**94.3**	**113.9**
Capex	0.0	0.0	0.0	0.0	0.0
Acquisitions & investments	(12.1)	(732.1)	(5.0)	(650.0)	(10.0)
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	**(12.1)**	**(732.1)**	**(5.0)**	**(650.0)**	**(10.0)**
Dividends paid	(32.7)	(50.9)	(56.4)	(91.5)	(96.3)
Interest expense	0.0	0.0	0.0	0.0	0.0
Change in debt	0.2	384.6	0.0	208.7	0.0
Equity raised / (purchased)	0.0	0.0	0.0	0.0	0.0
Other financial activities	0.0	361.8	0.0	0.0	0.0
CF from financing activities	**(32.5)**	**695.4**	**(56.4)**	**117.1**	**(96.3)**
Effect of exchange rate changes	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Net cash flow	**(4.5)**	**33.9**	**24.1**	**(438.6)**	**7.6**

FYE 31 Dec	FY14A	FY15A	FY16E	FY17E	FY18E
Key Ratios					
Growth ratios (%)					
Revenue growth	1.9	64.0	9.3	49.1	3.2
Net property income growth	0.2	69.3	14.8	43.9	3.3
Core net profit growth	(1.1)	58.1	11.1	52.6	5.3
Distributable income growth	(1.1)	58.1	11.1	52.6	5.3
Profitability ratios (%)					
Net property income margin	75.9	78.4	82.4	79.5	79.6
Core net profit margin	48.6	46.9	47.7	48.8	49.8
Payout ratio	86.1	84.8	84.6	90.0	90.0
DuPont analysis					
Total return margin (%)	48.6	46.9	47.7	48.8	49.8
Gross revenue/Assets (x)	0.1	0.1	0.1	0.1	0.1
Assets/Equity (x)	1.6	1.8	1.8	1.7	1.7
ROAE (%)	6.4	7.5	6.6	8.1	7.1
ROAA (%)	4.0	4.3	3.7	4.6	4.1
Liquidity & Efficiency					
Days receivable outstanding	22.4	18.5	16.4	11.0	10.6
Days payables outstanding	254.1	187.1	221.6	127.9	124.1
Dividend cover (x)	1.2	1.2	1.2	1.1	1.1
Current ratio (x)	2.0	3.2	1.9	2.0	1.6
Leverage & Expense Analysis					
Asset/Liability (x)	2.7	2.3	2.2	2.4	2.4
Net debt/equity (%)	52.1	71.3	67.9	60.1	59.6
Net interest cover (x)	3.6	3.0	3.0	3.4	3.5
Debt/EBITDA (x)	6.4	8.6	7.6	7.0	6.9
Capex/revenue (%)	0.0	0.0	0.0	0.0	0.0
Net debt/ (net cash)	281.8	644.9	615.9	815.0	807.4
Debt/Assets (x)	0.35	0.42	0.42	0.39	0.39

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

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 kllo@kimeng.com.hk
• Consumer Discretionary & Auto

Mitchell KIM
(852) 2268 0634 mitchellkim@kimeng.com.hk
• Internet & Telcos

Ning MA
(852) 2268 0672 ningma@kimeng.com.hk
• Insurance

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

Stefan CHANG, CFA
(852) 2268 0675 stefanchang@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
• SMID 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 joshuatan@maybank-ke.com.sg
• REITs (Retail, Industrial)

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

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

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

Pandu ANUGRAH
(62) 21 8066 8688
pandu.anugrah@maybank-ke.co.id
• Infra • Construction • Transport• Telcos

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

Adhi TASMIN
(62) 21 8066 8694
adhi.tasmin@maybank-ke.co.id
• Plantations

Anthony LUKMAWIJAYA
(62) 21 8066 8690
anthony.lukmawijaya@maybank-ke.co.id
• Aviation

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_rodrigo@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

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

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

Yupapan POLPORNPRASERT
(66) 2658 6300 ext 1394
yupapan.p@maybank-ke.co.th
• Oil & Gas

Tanawat RUENBANTERNG
(66) 2658 6300 ext 1395
Tanawat.R@maybank-ke.co.th
• Banks & Diversified Financials

Sukit UDOMSIRIKUL *Head of Retail Research*
(66) 2658 6300 ext 5090
Sukit.u@maybank-ke.co.th

Mayuree CHOWVIKRAN
(66) 2658 6300 ext 1440
mayuree.c@maybank-ke.co.th
• Strategy

Padon VANNARAT
(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

Suttatip PEERASUB
(66) 2658 6300 ext 1430
suttatip.p@maybank-ke.co.th
• Media • Commerce

Sutthichai KUMWORACHAI
(66) 2658 6300 ext 1400
sutthichai.k@maybank-ke.co.th
• Energy • Petrochem

Termporn TANTIVIVAT
(66) 2658 6300 ext 1520
termporn.t@maybank-ke.co.th
• Property

Jaroonpan WATTANAWONG
(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 Quang Trung, CFA, Deputy Manager, Institutional Research
(84) 8 44 555 888 x 8180
trung.thai@maybank-kimeng.com.vn
• Real Estate • Construction • Materials

Le Nguyen Nhat Chuyen
(84) 8 44 555 888 x 8082
chuyen.le@maybank-kimeng.com.vn
• Oil & Gas

NGUYEN Thi Ngan Tuyen, *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) 4 44 555 888 x 8208
diep.trinh@maybank-kimeng.com.vn
• Technology • Utilities • Construction

PHAM Nhat Bich
(84) 8 44 555 888 x 8083
bich.pham@maybank-kimeng.com.vn
• Consumer • Manufacturing • Fishery

NGUYEN Thi Sony Tra Mi
(84) 8 44 555 888 x 8084
mi.nguyen@maybank-kimeng.com.vn
• Port operation • Pharmaceutical
• Food & Beverage

TRUONG Quang Binh
(84) 4 44 555 888 x 8087
binh.truong@maybank-kimeng.com.vn
• Rubber plantation • Tyres and Tubes • Oil&Gas

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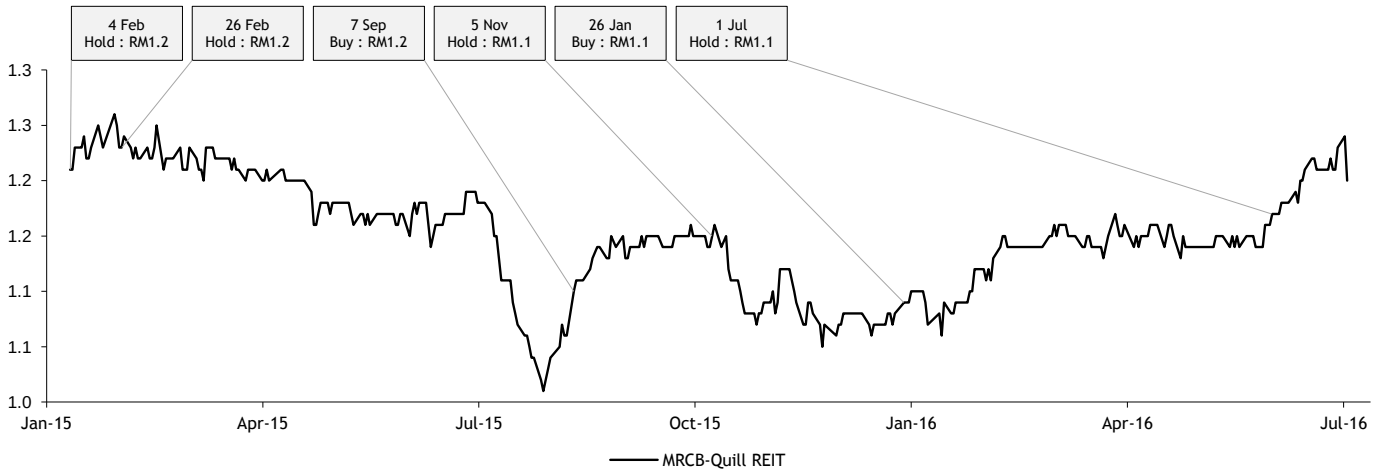
Historical recommendations and target price: MRCB-Quill REIT (MQREIT MK)



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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 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

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, 22nd Floor
Jl. Asia Afrika No. 8
Gelora Bung Karno, Senayan
Jakarta 10270, Indonesia

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

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

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

Thailand
Maybank Kim Eng Securities (Thailand) Public Company Limited
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)

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

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

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
Harianto Liong
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

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

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

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