Oiltek International Ltd

Riding major capex cycles

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SINGAPORE | ENGINEERING | INITIATION

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- The order book for Oiltek has been growing at a 50% CAGR over the past four years. FY24e is poised to be a fifth straight year of record orders. Oiltek secured new orders last week, which boosted its order book by around 30%, currently RM400mn or two times FY23 revenue.
- FY23 net profit jumped 51% to RM19.1mn on the back of strong order wins of RM322mn (FY22: RM196mn). We believe the company is riding multiple capex cycles. These include growth in biodiesel capacity in Malaysia and Indonesia, higher value-added products downstream, and expansion of customer base in Africa and Latin America. The largest growth opportunity will be the increasing use of sustainable aviation fuel oil using palm oil effluents in SE Asia.
- Oiltek has an enviable 31% ROE business that is asset-light and backed by net cash of RM132mn (~70% market cap). Its high returns stem from selling proprietary know-how and successfully designing, operating, and commissioning customer plants with a 45-year track record of project completions. We initiate coverage with a target price of S$0.70, or 15x PE FY24e. There are no direct comparables. We peg Oiltek at a discount to the engineering sector, which trades at 24x forward PE. FY24e EV/EBITDA is 1x.

Background

Established in 1980, Oiltek is a design and engineering specialist for vegetable oil refineries and processing plants for major agricultural commodities, including palm (80-90%), soybean, and rapeseed. Core production processes or products include palm oil refining, fractionalization, specialty fats, biodiesel, and potentially hydrogenated vegetable oil (HVO) for sustainable aviation fuel (SAF). The company is based in Malaysia and was listed on the Catalist in March 2022. Oiltek has customers in more than 34 countries, including major listed plantation companies. Indonesia accounted for 78% of its FY23 revenue.

Highlights

- **Riding multiple capex cycles.** Oiltek is dependent on customers' capex plans, especially in the palm oil sector. Its growth drivers include: i) higher in biodiesel blending in Malaysia from B10 (or 10% palm oil) to B20. This will increase the expected biodiesel tonnage to 1.8mn tonnes. The typical size of a biodiesel plant is 400k tonnes, implying additional four to five new plants; (ii) an increase in Indonesia biodiesel blend from B35 (since Aug23) to B40; iii) new biodiesel facilities nationwide in Indonesia and Malaysia for more comprehensive logistics coverage; iv) further downstream integration into higher value-added products, including specialty fast, animal feed, Rumen fats, cocoa butter equivalent and phytonutrients; v) Expansion of palm oil refining facilities and downstream diversification globally such as in Latin America.
- **The SAF bounty.** There is a growing demand for SAF. IATA projects SAF production will triple to 1.5mn tonnes in 2024. This would still be only 0.5% of aviation fuels in 2024. Announced SAF projects could reach 51mn tonnes by 2030. Many countries have mandated flights to use 3-10% of SAF by 2030. Oiltek has the solutions to treat palm oil mill effluent (POME) and used cooking oil as feedstock for the production of HVO. HVO is, in turn, the feedstock to produce SAF.
- **Asset-light, strong ROE and cash flow.** Oiltek's key assets are its proprietary process technologies and a 45-year record of completing projects. It outsources plant fabrication and installation work to third-party plants, which minimises minimizing capex needs. Oiltek generates an ROE of 31% despite net cash of RM132mn. The dividend yield was 5% in FY23. We expect dividends to grow by 13% in FY24e.

BUY (Initiation)

CLOSING PRICE	SGD 0.365
FORECAST DIV	SGD 0.018
TARGET PRICE	SGD 0.700
TOTAL RETURN	**96.7%**

COMPANY DATA

Bloomberg CODE:	OTEK SP Equity
O/S SHARES (MN) :	143.0
MARKET CAP (USD mn / SGD mn) :	39 / 52
52 - WK HI/LO (SGD) :	0.39 / 0.19
3M Average Daily T/O (mn) :	0.19

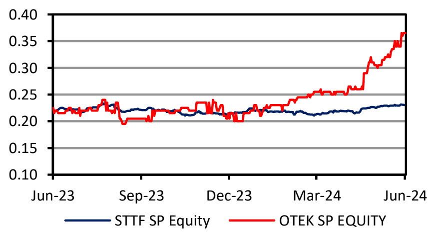
MAJOR SHAREHOLDERS

Koh Brothers Group Ltd	68.1%
Yong Khai Weng	6.3%

PRICE PERFORMANCE (%)

	1MTH	3MTH	YTD
COMPANY	19.7	50.6	74.6
STTF RETURN	1.9	8.6	5.4

PRICE VS. STTF



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec, RM (mn)	FY22	FY23	FY24e	FY25e
Revenue	164	201	250	320
EBITDA	13.9	23.0	29.3	37.6
Net Profit	12.7	19.1	23.2	29.2
EPS (SGD cents)	2.6	3.8	4.7	5.9
P/E (X)	14.0	9.5	7.8	6.2
Dividend Yield	3.3%	4.4%	4.9%	5.5%
ROE	28.8%	31.5%	29.7%	28.6%
ROA	12.4%	12.4%	11.5%	12.2%

Source: Company, PSR

VALUATION METHOD

15x PE Multiple FY24e

Paul Chew (+65 6212 1851)
Head of Research
paulchewkl@phillip.com.sg

Background

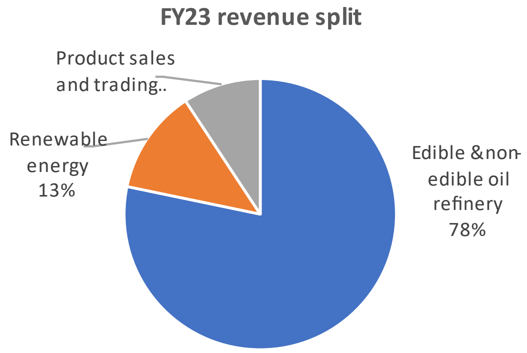
Oiltek is a design and engineering specialist for vegetable oil refineries and processing systems for major agricultural commodities, including palm, soybean, and rapeseed. These refineries produce edible and non-edible oil, related downstream products, and renewable energy such as biodiesel and biogas. Its key customers are major listed plantation companies.

Edible and non-edible oil refinery construction and upgrade accounted for 78% of revenue share in FY23 (Figure 1). Still, renewable energy, comprising biodiesel and biogas plants, grew at a faster rate of 83% YoY (Figure 2).

Oiltek has the technology solution to process waste fats/oil, such as palm oil mill effluent (POME) and used cooking oil (UCO), as well as other vegetable oil-based raw materials, into the feedstock for production of hydrogenated vegetable oil (HVO), which is used as sustainable aviation fuel. Its process technology complies with the International Sustainability and Carbon Certification (ISCC). Oiltek has delivered its first HVO feedstock treatment plant that uses POME to a customer in Malaysia.

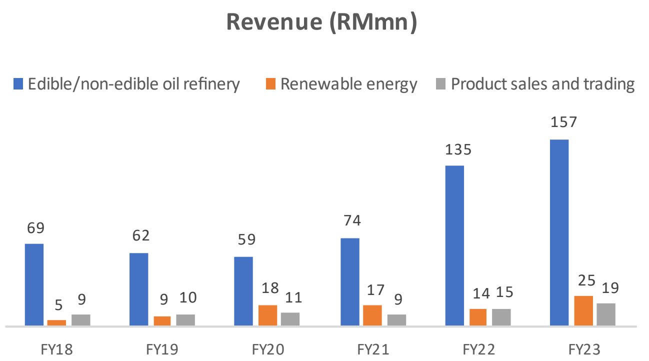
Some of its notable customers include Wilmar International Limited, Sarawak Oil Palms Bhd, Bunge Loders Croklaan, FGV Holdings Bhd, Sime Darby Plantation Bhd, and PT Sinar Mas Agro Resources and Technology Tbk.

Figure 1: Edible and non-edible oil refinery takes 78% of revenue share



Source: PSR, Company

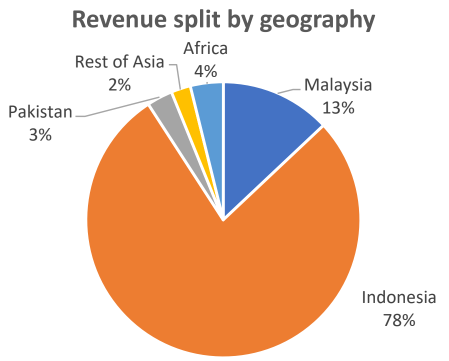
Figure 2: Renewable energy grew the fastest at a 5-year CAGR of 39%



Source: PSR, Company

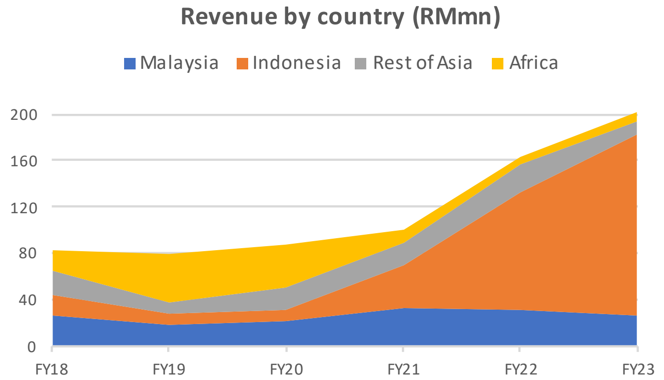
The two largest markets are Indonesia and Malaysia (Figure 3), the largest palm oil producers globally. The two countries are advocating the use of biodiesel produced from oil palm.

Figure 3: Indonesia is its largest and fastest-growing market



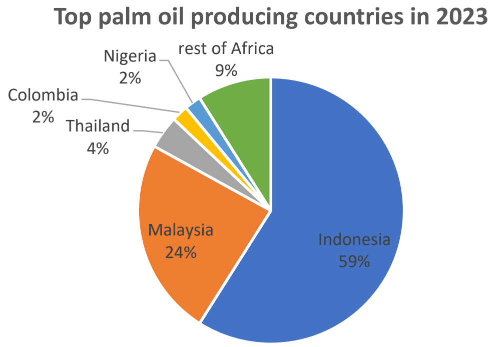
Source: PSR, Company

Figure 4: Projects in Indonesia took off in FY21



Source: PSR, Company

Figure 5: Indonesia accounts for 59% of the world's palm oil production



Source: USDA

Revenue

Oiltek's revenue is from engineering, procurement, designing, construction and commissioning (EPCC), upgrading, and turnkey engineering. Revenue is split by industry: edible oil and non-edible oil refinery (78% of FY23 revenue), renewable energy (13%), and trading (9%).

Revenue is recognised based on a percentage completion method. The typical revenue recognition cycle is 18-24 months. Between 7-8 months for fabrication and delivery of the equipment and 8-12 months for installation. Payment terms are usually 10-30% downpayment, another 50-60% during delivery and 5-15% upon commissioning. The warranty period may be 5%. Contract liabilities on the balance sheet are essentially down

3 types of revenue

- engineering, procurement, designing, construction and commissioning (EPCC);
- upgrading and retrofitting of existing facilities;
- turnkey infrastructure engineering

payments for projects that have not been completed. In comparison, contract assets are work delivered but not billed.

Cost

Oiltek's cost of sales is largely raw materials, equipment, and subcontracting costs (90-95%). The company outsources the subcontracting work rather than fabricating equipment in-house. Some of the parts Oiltek will purchase include membrane filters, heat exchangers, vessel fabrication and pressurised vessels. A sub-contract is Bursa Malaysia listed Kawan Renergy. Gross margins range between 20-23%. Margins depend on region and type of product.

Order Book

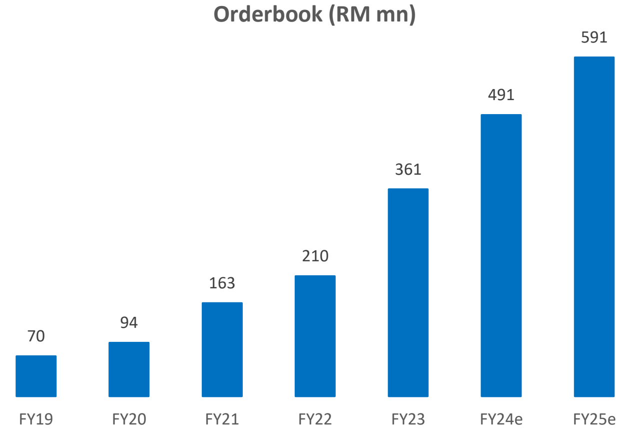
The order book at the end of December was RM361mn (Figure 6). Order wins rose 64% in FY23 to RM322mn. On 3 June, the company announced new contracts totalling RM94.8mn* from Malaysia, Indonesia, and Kenya. The order book now stands at a record RM400.5mn.

**The type of contracts are new crude palm oil pretreatment plant and a new biodiesel plant, one new downstream premium specialty animal feed product processing plant, the design, fabrication, delivery, testing & commissioning of crystallizer loops for a dry fractionation plant and the design, fabrication, delivery, testing & commissioning of one new 500MTD Alkaline Close Loop Vacuum System.*

We believe some of the drivers in growing the order book are:

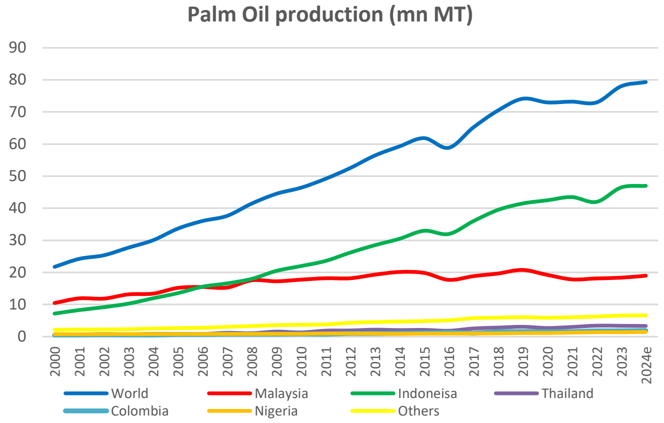
i. Increase in biodiesel capacity in Malaysia from B10 (or 10% palm oil blend) to B20. Malaysia is way behind Indonesia's current B35. This will increase the expected biodiesel tonnage to 1.8mn tonnes. The typical size of a biodiesel plant is 400k tonnes, implying an additional four to five new plants;
ii. Increase in Indonesia biodiesel from B35 (since Aug23) to B40;
iii. New biodiesel facilities nationwide in Indonesia and Malaysia for more comprehensive logistic coverage;
iv. Further downstream integration into higher value-added products, including specialty fat, animal feed, Rumen Fat, cocoa butter equivalent, and phytonutrients;
v. Expansion of palm oil refining facilities and downstream diversification globally, such as in Latin America. World production is growing by around 3.3% p.a. (Figure 7);
vi. Oiltek is expanding its scope of work by including turnkey solutions for seamless project and timeliness execution.

Figure 6: On track for record order book for the fifth year



Source: PSR, Company

Figure 7: World palm oil production growing at a 10-year CAGR of 3.3% p.a.

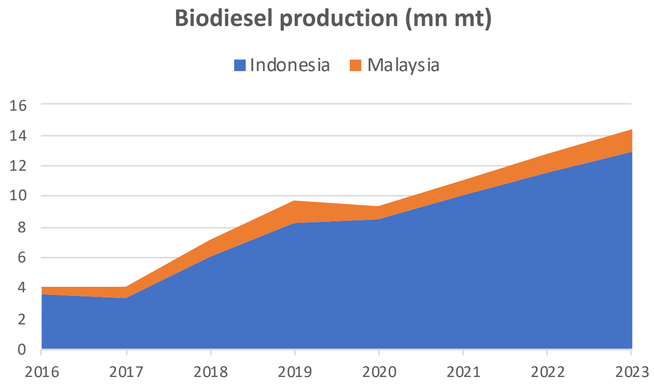


Source: USDA

Biodiesel mandate

Driven by national biodiesel mandates, biodiesel production has risen by a 6-year CAGR of 23.3% in Indonesia and Malaysia (Figure 8).

Figure 8: Biodiesel output growing strongly



Source: MPA, MPOB, APROBI

Indonesia's national biodiesel mandate aims to blend diesel with palm-based Fatty Acid Methyl Ester (FAME). The blending rate was raised to 35% across all regions in Aug 2023, and targeting B40 in the future. The objective is to reduce fuel imports, generate domestic demand for palm oil, and cut emissions.

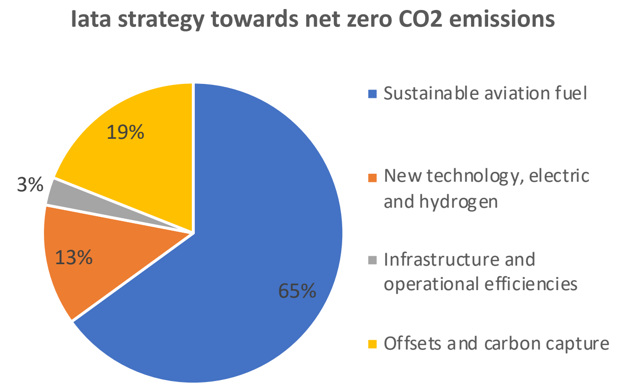
Malaysia has a similar proposed B20 mandate for the transport sector. However, this has not yet been implemented nationwide due to limited blending facilities. If the B20 mandate is met, FY23 biodiesel production could be 79% higher at 2.5mn MT, according to the Malaysian Biodiesel Association.

We expect more investments in biodiesel plants as each state seeks to be self-reliant in biodiesel supply. Under the 12th Malaysian plan, the transport sector must implement the B30 blending mandate by 2025.

Sustainable aviation fuel

The international aviation industry targets to reach net zero CO2 emissions by 2050. This will require a ramp-up in the production of sustainable aviation fuel, which could contribute around 65% of the reduction in emissions needed by aviation, according to Iata (Figure 9). Many countries have mandated flights to use 3-10% of SAF by 2030.

Figure 9: IATA strategy towards net zero CO2 emissions



Source: Iata

SAF is a liquid fuel currently used in commercial aviation. It can reduce CO_2 emissions by up to 80%. It can be produced from various sources, including waste oil and fats, green and municipal waste, and non-food crops.

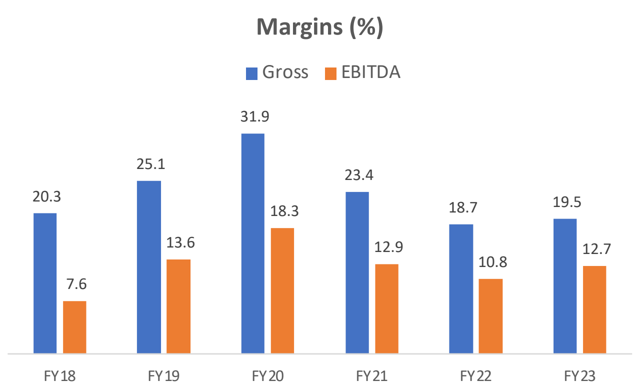
Hydrogenated vegetable oil (HVO), also known as hydroprocessed esters and fatty acids (HEFA), is one of the frontrunner technical pathways for SAF output in the near term. HVO is a synthetic paraffinic diesel reprocessed from vegetable oils or waste with added hydrogen. Unlike previous biofuels, it is a drop-in replacement fuel that can be used without modifying existing engines. Europe is currently the largest producer of HVO.

Oiltek has solutions to treat palm oil mill effluent (POME) and used cooking oil, as well as any other vegetable oil-based raw materials, as feedstock in the production of HVO. Its solutions comply with the International Sustainability & Carbon Certification. It delivered its first HVO feedstock treatment plant, which uses POME, to a customer in Malaysia. We expect more order wins for these plants in tandem with the growth in SAF consumption. Malaysia exports 415,520 MT of POME to the EU. There is an opportunity to add value to these exports and turn them into valuable SAF.

Financials

Gross margins were lower in the last two years (Figure 10) as Oiltek took on more turnkey projects but outsourced the plant fabrication and installation work to third-party contractors.

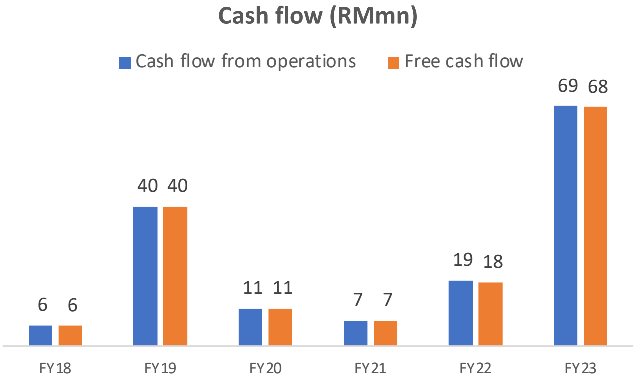
Figure 10: Margins contracted due to a higher proportion of turnkey projects



Source: PSR, Company

The asset-light and strong cash flow generative model lift ROE to 31% and free-cash flow of RM69mn in FY23. Capex is only RM300,000 to RM400,000 per year.

Figure 11: Low capex needs to lift free cash flow



Source: PSR, Company

Valuations

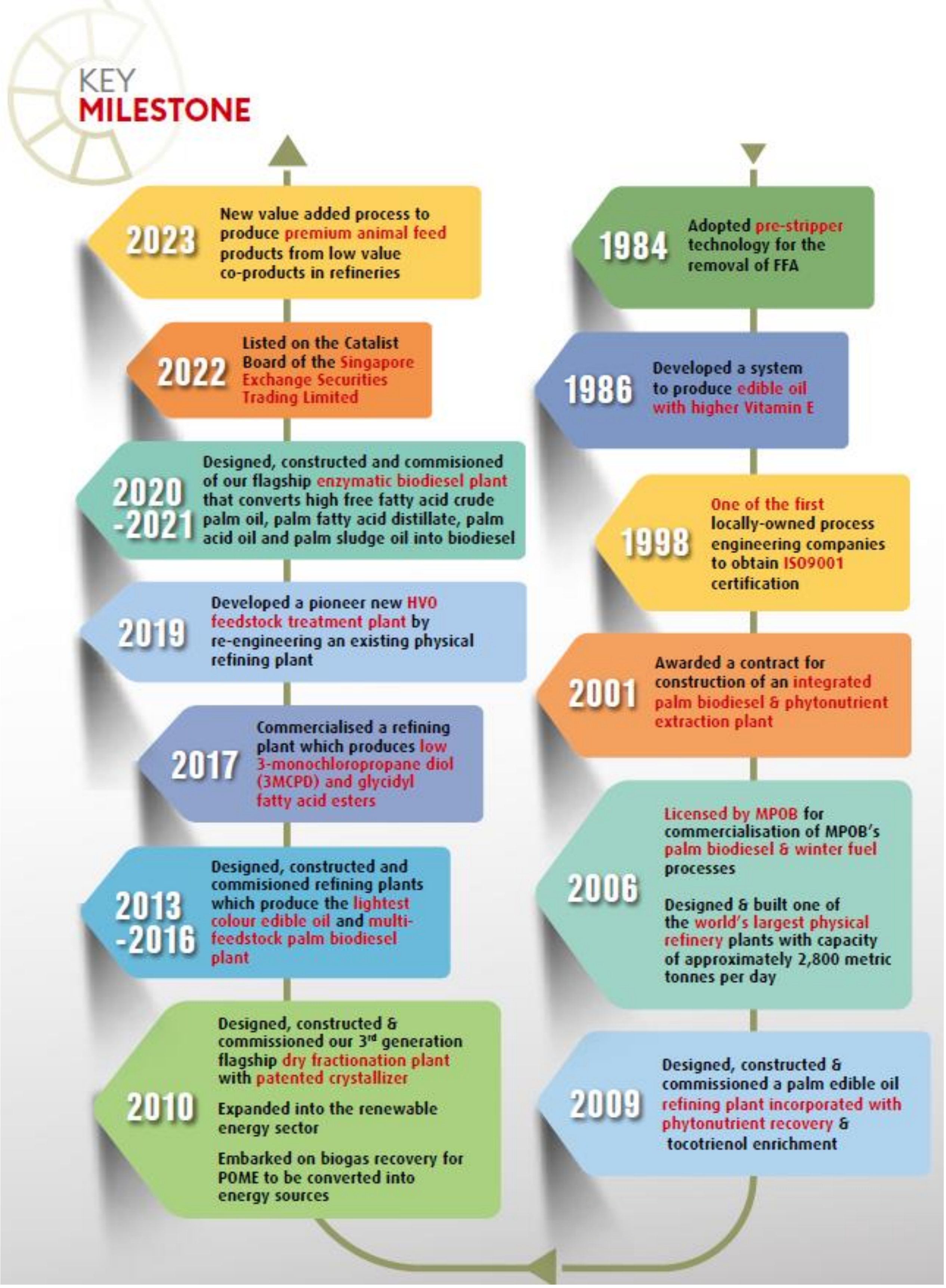
There are no direct listed comparables to Oiltek. We value Oiltek based on proxies to the industry. The closest is the industrial process equipment (boilers, heaters, heat exchangers, and pressure vessels) fabricator Kawan Renergy, which is also an equipment supplier to Oitek. BM GreenTech also has a subsidiary, Boilermech, that manufactures, repairs, and services boilers. Kinergy Advancement is involved in renewable energy EPCC and ownership of such assets.

Figure 12: Malaysia equipment maker proxies trading at 24x PE forward

Company	1 Mth Perf.	3 Mth Perf.	YTD Perf.	PSR Rec.	Share Px Local Crcy	Mkt. Cap. (US$ m)	PE Yr 0	PE Yr + 1	PE Yr + 2	Dividend Yield	EV/ EBITDA (x)	ROE	Net Profit (RM mn)
Singapore													
Oiltek	19.7%	43.1%	65.9%	BUY	0.365	39	9.5	7.8	6.2	4.4%	2.2	31.5%	19.1
Malaysia (proxy)													
Kinergy Advancement	0.0%	0.0%	-5.1%	-	0.37	157	26.8	n.a.	n.a.	0.0%	18.2	16.2%	15.8
BM Greentech	31.0%	76.5%	82.3%	-	1.65	182	25.3	22.6	21.3	0.4%	14.8	13.5%	33.5
Kawan Renergy	165.0%	165.0%	165.0%	-	0.80	93	32.9	28.6	23.5	0.0%	20.4	27.0%	13.2
Malaysia Total	48.7%	67.8%	68.4%			431	27.2	24.3	22.0	0.2%	17.2	17.4%	62.5

Source: PSR, Company # Kawan Renergy IPO was on 29May24

APPENDIX 1: KEY MILESTONE



Source: PSR, Company 2023 Annual Report

APPENDIX 2: > 43 YEAR TRACK RECORD

Source: PSR, Company 2023 Annual Report

PhillipCapital

Financials

Income Statement

Y/E Dec, RM mn	FY21	FY22	FY23	FY24e	FY25e
Revenue	**100.6**	**163.7**	**201.1**	**250.4**	**319.9**
Gross profit	23.6	30.6	39.2	50.3	65.6
EBITDA	**12.4**	**13.9**	**23.0**	**29.3**	**37.6**
Depreciation & amortisation	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
EBIT	**12.3**	**13.7**	**22.8**	**29.0**	**37.4**
Other income	0.1	2.2	1.3	1.7	1.3
Other gain / (losses)	0.7	1.8	1.4	0.2	0.2
Profit before tax	13.0	17.7	25.5	31.0	38.9
Taxation	(3.3)	(5.0)	(6.4)	(7.7)	(9.7)
Minority intrest	-	-	-	-	-
PATMI	**9.7**	**12.7**	**19.1**	**23.2**	**29.2**

Per share data (SGD Cents)

Y/E Mar	FY21	FY22	FY23	FY24e	FY25e
EPS, Reported	2.31	2.61	3.84	4.66	5.86
DPS	1.09	1.20	1.60	1.80	2.00
BVPS	0.08	0.11	0.14	0.18	0.23

Cash Flow

Y/E Dec, RM mn	FY21	FY22	FY23	FY24e	FY25e
<u>CFO</u>					
Profit before tax	**13.0**	**17.7**	**25.5**	**31.0**	**38.9**
Adjustments	0.4	0.9	(2.6)	(1.5)	(1.1)
WC changes	(2.7)	4.2	51.0	(2.1)	5.7
Cash generated from ops	10.7	22.8	73.9	27.4	43.5
Tax paid	(3.5)	(4.2)	(5.1)	(6.0)	(8.4)
Cashflow from ops	**7.2**	**18.6**	**68.8**	**21.4**	**35.1**
<u>CFI</u>					
CAPEX, net	(0.0)	(0.4)	(0.3)	(0.4)	(0.5)
Others	-	-	0.0	-	-
Cashflow from investments	**(0.0)**	**(0.4)**	**(0.3)**	**(0.4)**	**(0.5)**
<u>CFF</u>					
Share issuance, net	-	16.0	-	-	-
Dividends	(14.4)	(8.9)	(5.9)	(2.3)	(2.6)
Others	(0.9)	(0.5)	-	-	-
Cashflow from financing	**(15.2)**	**6.6**	**(5.9)**	**(2.3)**	**(2.6)**
Net change in cash	(8.1)	24.8	62.6	18.7	32.0
CCE, end	**42.9**	**67.4**	**132.5**	**151.2**	**183.2**

Balance Sheet

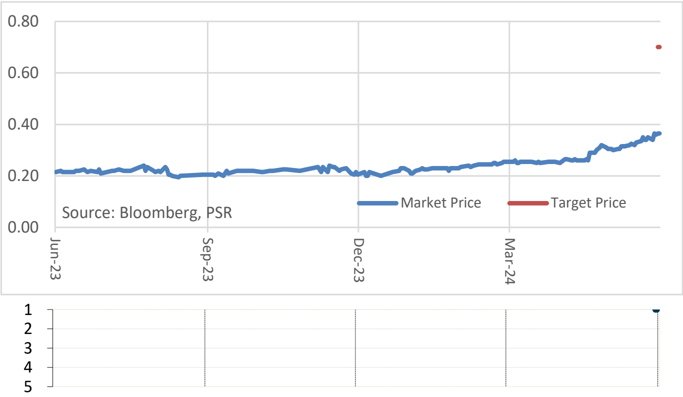
Y/E Dec, RM mn	FY21	FY22	FY23	FY24e	FY25e
ASSETS					
Trade and other receivables	17.0	11.4	26.9	39.5	50.5
Cash	42.9	67.4	132.5	151.2	183.2
Inventories	9.0	6.0	5.7	16.7	21.4
Others	10.3	34.2	16.4	6.5	2.3
Total current assets	**79.1**	**119.0**	**181.5**	**213.9**	**257.3**
PPE	2.9	3.2	3.3	3.5	3.8
Others	0.2	0.3	0.5	0.5	0.5
Total non-current assets	**3.1**	**3.5**	**3.8**	**4.0**	**4.2**
Total Assets	**82.2**	**122.5**	**185.2**	**217.9**	**261.6**
LIABILTIES					
Accounts payable	31.2	44.4	38.4	50.1	67.2
Bank borrowings	-	-	-	-	-
Other payables	15.9	23.1	77.4	77.4	77.4
Others	0.8	1.6	1.7	1.7	1.7
Total current liabilities	**47.9**	**69.0**	**117.5**	**129.2**	**146.3**
Total non-current liabilities	-	-	-	-	-
Total Liabilities	**47.9**	**69.0**	**117.5**	**129.2**	**146.3**
Equity					
Share capital	83.9	98.6	98.6	98.6	98.6
Shareholder Equity	**34.4**	**53.5**	**67.7**	**88.7**	**115.3**

Valuation Ratios

Y/E Dec	FY21	FY22	FY23	FY24e	FY25e
P/E (X)	15.8	14.0	9.5	7.8	6.2
P/B (X)	4.5	3.4	2.7	2.1	1.6
EV/EBITDA (X)	8.9	8.3	2.2	1.0	0.0
Dividend Yield	3.0%	3.3%	4.4%	4.9%	5.5%
Growth & Margins					
<u>Growth</u>					
Revenue	15.0%	62.7%	22.8%	24.5%	27.7%
EBITDA	-23.7%	11.8%	65.6%	27.4%	28.7%
EBIT	-23.4%	11.7%	66.1%	27.5%	28.8%
PATMI	-19.5%	30.5%	50.9%	21.5%	25.7%
<u>Margins</u>					
Gross margin	23.4%	18.7%	19.5%	20.1%	20.5%
EBITDA margin	12.3%	8.5%	11.4%	11.7%	11.8%
EBIT margin	12.2%	8.4%	11.3%	11.6%	11.7%
Net profit margin	9.6%	7.7%	9.5%	9.3%	9.1%
Key Ratios					
ROE	28.4%	28.8%	31.5%	29.7%	28.6%
ROA	13.0%	12.4%	12.4%	11.5%	12.2%
Net Gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Net Debt/EBITDA (X)	n.a.	n.a.	n.a.	n.a.	n.a.

Source: Company, Phillip Securities Research (Singapore) Estimates

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

Contact Information (Singapore Research Team)

Head of Research
Paul Chew – paulchewkl@phillip.com.sg

Research Admin
Qystina Azli - qystina@phillip.com.sg

Technical Analyst
Zane Aw – zaneawyx@phillip.com.sg

Property | REITs
Darren Chan – darrenchanrx@phillip.com.sg

Banking & Finance
Glenn Thum – glennthumjc@phillip.com.sg

Credit Analyst
Shawn Sng – shawnsngkh@phillip.com.sg

Property | REITs
Liu Miaomiao – liumm@phillip.com.sg

US Tech Analyst (Software/Services)
Ambrish Shah – amshah@phillipventuresifsc.in

US Tech Analyst (Digital Entertainment/Semicons)
Jonathan Woo – jonathanwookj@phillip.com.sg

US Tech Analyst (Hardware/E-commerce)
Helena Wang – helenawang@phillip.com.sg

Contact Information (Regional Member Companies)

SINGAPORE
Phillip Securities Pte Ltd
Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel +65 6533 6001
Fax +65 6535 6631
Website: www.poems.com.sg

MALAYSIA
Phillip Capital Management Sdn Bhd
B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel +603 2162 8841
Fax +603 2166 5099
Website: www.poems.com.my

HONG KONG
Phillip Securities (HK) Ltd
11/F United Centre 95 Queensway
Hong Kong
Tel +852 2277 6600
Fax +852 2868 5307
Websites: www.phillip.com.hk

JAPAN
Phillip Securities Japan, Ltd.
4-2 Nihonbashi Kabuto-cho Chuo-ku,
Tokyo 103-0026
Tel +81-3 3666 2101
Fax +81-3 3666 6090
Website: www.phillip.co.jp

INDONESIA
PT Phillip Securities Indonesia
ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel +62-21 5790 0800
Fax +62-21 5790 0809
Website: www.phillip.co.id

CHINA
Phillip Financial Advisory (Shanghai) Co Ltd
No 550 Yan An East Road,
Ocean Tower Unit 2318,
Postal code 200001
Tel +86-21 5169 9200
Fax +86-21 6351 2940
Website: www.phillip.com.cn

THAILAND
Phillip Securities (Thailand) Public Co. Ltd
15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel +66-2 6351700 / 22680999
Fax +66-2 22680921
Website www.phillip.co.th

FRANCE
King & Shaxson Capital Limited
3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel +33-1 45633100
Fax +33-1 45636017
Website: www.kingandshaxson.com

UNITED KINGDOM
King & Shaxson Capital Limited
6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel +44-20 7426 5950
Fax +44-20 7626 1757
Website: www.kingandshaxson.com

UNITED STATES
Phillip Capital Inc
141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1-312 356 9000
Fax +1-312 356 9005
Website: www.phillipusa.com

AUSTRALIA
Phillip Capital Limited
Level 10, 330 Collins Street
Melbourne, Victoria 3000, Australia
Tel +61-03 8633 9803
Fax +61-03 8633 9899
Website: www.phillipcapital.com.au

CAMBODIA
Phillip Bank Plc
Ground Floor of B-Office Centre,#61-64,
Norodom Blvd Corner Street 306,Sangkat
Boeung Keng Kang 1, Khan Chamkamorn,
Phnom Penh, Cambodia
Tel: 855 (0) 7796 6151/855 (0) 1620 0769
Website: www.phillipbank.com.kh

INDIA
PhillipCapital (India) Private Limited
No.1, 18th Floor, Urmi Estate
95, Ganpatrao Kadam Marg
Lower Parel West, Mumbai 400-013
Maharashtra, India
Tel: +91-22-2300 2999 / Fax: +91-22-2300 2969
Website: www.phillipcapital.in

TURKEY
PhillipCapital Menkul Degerler
Dr. Cemil Bengü Cad. Hak Is Merkezi
No. 2 Kat. 6A Caglayan
34403 Istanbul, Turkey
Tel: 0212 296 84 84
Fax: 0212 233 69 29
Website: www.phillipcapital.com.tr

DUBAI
Phillip Futures DMCC
Member of the Dubai Gold and
Commodities Exchange (DGCX)
Unit No 601, Plot No 58, White Crown Bldg,
Sheikh Zayed Road, P.O.Box 212291
Dubai-UAE
Tel: +971-4-3325052 / Fax: + 971-4-3328895

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