

BUY (Unchanged)

Change in Numbers

TP: Bt 26.00

Upside : 31.3%

(From: Bt 24.00)

22 JUNE 2021

Small Cap Research

Ch. Karnchang Pcl (CKTB)

Factoring in West Orange Line

Factoring in the West Orange Line project, we raise our new work value for CK by 100% in 2022F, our earnings by 1-7% in 2022-23F, and TP to Bt26. With the highest earnings growth of 29-120% in 2021-23F among peers while its shares are still trading at a 48% discount to its associates' market value, CK is now our top sector pick.

**SAKSID PHADTHANANARAK**

662 – 779 9112

saksid.pha@thanachartsec.co.th

The West Orange Line project

The bid for the construction and operation of the West Orange Line project (Bt127bn) opened in late 2020 but it was cancelled due to a change in the bidding method by the project owner, the Mass Rapid Transit Authority (MRTA), causing one bidder to take the case to court. The court's decision is still pending but we expect MRTA to relaunch the bid by next year as **1)** we see infrastructure projects as one of the government's economic stimulus measures after COVID subsidies, **2)** the West Orange Line will be implemented under the public-private partnership scheme, so it will not burden the government's budget and **3)** the bidding delay will mean there is no operator for the East Orange Line which is due to be completed in 2023 and the government will have to pay Bt150-200m a year for maintenance.

Raising our TP to Bt26; reaffirming BUY call

We take the view that BEM will win this project given its operational advantages (it is the only subway operator in Thailand), its lower costs (economies of scale) and construction capabilities (its parent firm, CK, is one of two contractors that have experience in building subways). BEM would then subcontract the construction work to CK. Factoring in this Bt96bn of work, we raise our earnings for CK by 1-7% over 2022-23F. Rolling over of the base year in our model to 2022F, we lift our DCF-derived SOTP-based 12-month TP to Bt26/share from Bt24 and reaffirm our BUY rating on CK. Please note that we assume no new infrastructure project bids open in 2023F due to the election year but that accumulated backlog value in 2021-22F is large enough to still drive CK's earnings growth by 29% in 2023F.

48% discount to associates' value

CK is now our top sector pick as, among the contractors we cover, we estimate it to offer the highest earnings growth of 29-120% in 2021-23F driven by its high new work value and earnings contributions from its associates. Its valuation also looks cheap to us with the shares trading at a 48% discount to its associates' market value (see Exhibit 5). We believe this is because of operating losses of the construction business. However, with the construction business's earnings recovery driven by high new work value, we expect the discount to narrow.

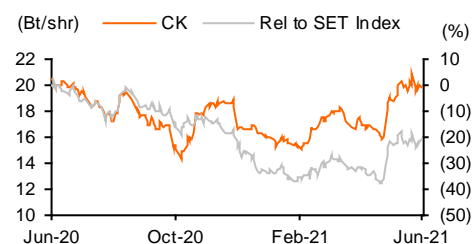
Short-term catalyst

We expect a short-term catalyst for contractor stocks including CK from the MRTA scheduling to open bids for the South Purple Line project (Bt108bn). The announcement of the term of reference (TOR) is planned for 5 July this year, the submission of bids in October and the announcement of the winners early next year. We have factored in CK winning 25% of the value.

COMPANY VALUATION

| Y/E Dec (Bt m) | 2020A | 2021F | 2022F | 2023F |
|-------------------|--------|---------|--------|--------|
| Sales | 16,941 | 13,842 | 18,722 | 26,611 |
| Net profit | 612 | 742 | 1,099 | 1,416 |
| Consensus NP | — | 878 | 1,462 | 1,872 |
| Diff frm cons (%) | — | (15.4) | (24.8) | (24.4) |
| Norm profit | 337 | 742 | 1,099 | 1,416 |
| Prev. Norm profit | — | 743 | 1,090 | 1,323 |
| Chg frm prev (%) | — | (0.1) | 0.8 | 7.0 |
| Norm EPS (Bt) | 0.20 | 0.44 | 0.65 | 0.84 |
| Norm EPS grw (%) | (65.0) | 120.3 | 48.1 | 28.8 |
| Norm PE (x) | 99.5 | 45.2 | 30.5 | 23.7 |
| EV/EBITDA (x) | 227.7 | 1,022.7 | 205.4 | 86.9 |
| P/BV (x) | 1.3 | 1.3 | 1.2 | 1.2 |
| Div yield (%) | 1.0 | 0.9 | 1.3 | 1.7 |
| ROE (%) | 1.3 | 2.8 | 4.1 | 5.1 |
| Net D/E (%) | 131.8 | 124.6 | 115.0 | 104.5 |

PRICE PERFORMANCE



COMPANY INFORMATION

| | |
|-----------------------------|-------------------------|
| Price as of 21-Jun-21 (Bt) | 19.80 |
| Market Cap (US\$ m) | 1,066.4 |
| Listed Shares (m shares) | 1,693.9 |
| Free Float (%) | 65.1 |
| Avg Daily Turnover (US\$ m) | 9.1 |
| 12M Price H/L (Bt) | 21.00/14.30 |
| Sector | Construction |
| Major Shareholder | Trivisvavet group 38.5% |

Sources: Bloomberg, Company data, Thanachart estimates

Ex 1: Key Assumption Changes

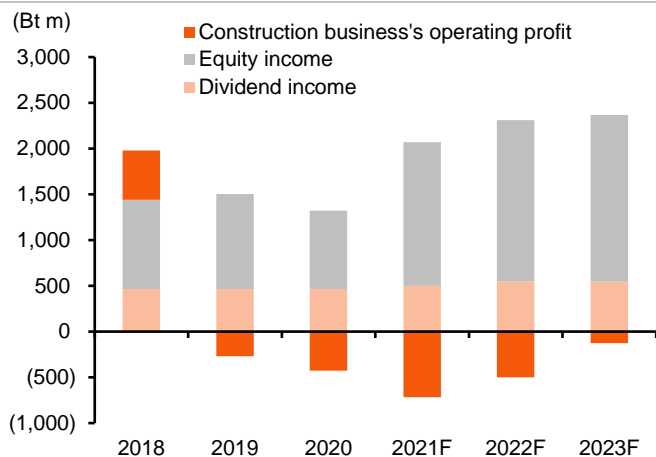
| | 2021F | 2022F | 2023F |
|-----------------------------------|-------|-------|--------|
| New work value (Bt bn) | | | |
| New | 29.0 | 200.0 | 10.0 |
| Old | 25.0 | 100.0 | 25.0 |
| Change (%) | 16.0 | 100.0 | (60.0) |
| Normalized earnings (Bt m) | | | |
| New | 742 | 1099 | 1,416 |
| Old | 743 | 1,090 | 1,323 |
| Change (pp) | (0.1) | 0.8 | 7.0 |

Sources: Thanachart estimates

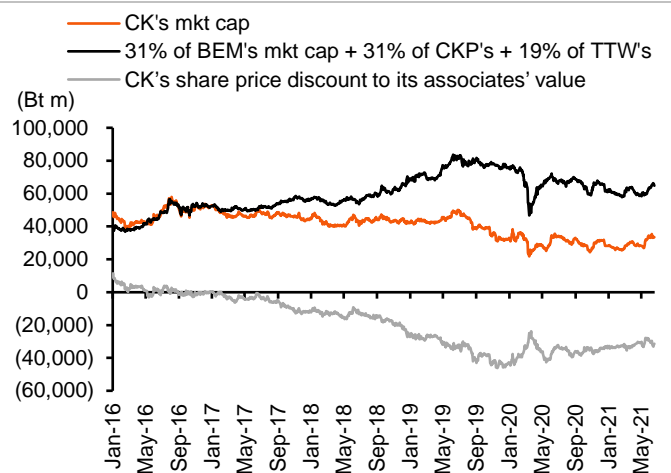
Ex 2: CK's Potential New Work Value

| Project | Construction Value (Bt bn) | Chance (%) | New work in 2021F (Bn) | New work in 2022F (Bn) | New work in 2023F (Bn) | New work in 2024F (Bn) |
|---|----------------------------|------------|------------------------|------------------------|------------------------|------------------------|
| Backlog value as of January 2021 | | | 26 | | | |
| Newly signed contracts | | | | | | |
| Water Transmission Tunnel | | | 5 | | | |
| Maintenance of BMCL's structures | | | 1 | | | |
| To be signed contracts | | | | | | |
| Double-track Denchai - Chiang Khong | | | 23 | | | |
| Potential projects | | | | | | |
| South Purple Line | 79 | 25 | - | 20 | - | - |
| West Orange Line | 96 | 100 | - | 96 | - | - |
| Red Line Extension | 67 | 25 | - | - | - | 17 |
| Double-track Chira – Ubon | 36 | 5 | - | 2 | - | - |
| Double-track Khon Kaen - Nong Khai | 25 | 5 | - | 1 | - | - |
| Luang Prabang Hydropower Plant | 81 | 100 | - | 81 | - | - |
| Others | - | - | - | - | 10 | 10 |
| Total new work value | 384 | | 29 | 200 | 10 | 27 |

Sources: Company data, Thanachart estimates

Ex 3: CK's Earnings Breakdown

Sources: Company data, Thanachart estimates

Ex 4: CK's Market Cap Vs. Its Associates' Market Cap

Source: Bloomberg

Ex 5: Our SOTP-Based Investment Equity Valuation Of CK

| | % holding | Our TP | Fair value (Bt m) | 30% discount* (Bt m) | Share price (Bt/share) | Market value (Bt m) |
|---|-----------|--------|-------------------|----------------------|------------------------|---------------------|
| TTW | 19.4% | 14.00 | 10,837 | 7,586 | 12.00 | 9,289 |
| BEM | 31.3% | 11.50 | 55,054 | 38,537 | 8.55 | 40,931 |
| CKP | 30.7% | 7.50 | 18,700 | 13,090 | 5.65 | 14,087 |
| Total | | | 84,590 | 59,213 | | 64,307 |
| Per CK share (Bt) | | | 50.0 | 35.0 | | 38.0 |
| Construction business's value (Bt) | | | | (9.0) | | |
| Our TP (Bt) | | | | 26.0 | | |

Sources: Company data, Thanachart estimates

Note: *We assume a holding company discount of 30% to our fair value of CK's associates.

Ex 6: EV Of Construction Business

| (Bt m) | 2022F | 2023F | 2024F | 2025F | 2026F | 2027F | 2028F | 2029F | 2030F | 2031F | 2032F | Terminal Value |
|------------------------------------|--------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|----------------|
| EBITDA | 317 | 728 | 901 | 1,177 | 1,522 | 1,635 | 1,317 | 1,085 | 726 | 771 | 807 | — |
| Free cash flow | 552 | 938 | 1,221 | 1,467 | 1,040 | 1,452 | 1,828 | 1,795 | 1,924 | 1,726 | 1,344 | 22,178 |
| PV of free cash flow | 550 | 815 | 990 | 1,089 | 717 | 929 | 1,086 | 990 | 985 | 786 | 566 | 9,335 |
| Risk-free rate (%) | 2.5 | | | | | | | | | | | |
| Market risk premium (%) | 8.0 | | | | | | | | | | | |
| Beta | 1.0 | | | | | | | | | | | |
| WACC (%) | 7.3 | | | | | | | | | | | |
| Terminal growth (%) | 2.0 | | | | | | | | | | | |
| Enterprise value - add investments | 18,838 | | | | | | | | | | | |
| Net debt (2021F) | 33,245 | | | | | | | | | | | |
| Minority interest | 436 | | | | | | | | | | | |
| Equity value | (14,843) | | | | | | | | | | | |
| # of shares (m) | 1,694 | | | | | | | | | | | |
| Equity value/share (Bt) | (8.8) | | | | | | | | | | | |

| Sum of the parts | % holding | (Bt m) |
|--|-----------|---------------|
| Enterprise value from construction business | | 18,838 |
| Investment equity value | | 59,213 |
| TTW | 19.4% | 7,586 |
| BEM | 31.3% | 38,537 |
| CKP | 30.7% | 13,090 |
| Total enterprise value | | 78,051 |
| (Less) Net debt | | (33,245) |
| (Less) Minority interest | | (436) |
| Total enterprise value | | 44,370 |
| # of shares (fully diluted) (m shares) | | 1,694 |
| Sum of the parts | | 26 |

Sources: Company data, Thanachart estimates

COMPANY DESCRIPTION

Ch. Karnchang Pcl (CK) is one of Thailand's leading contractors and basic infrastructure developers. It has more than 30 years of experience in constructing large-scale infrastructure, building complexes and general civil work. The company has also been investing in the government's concession projects in order to expand its operations and generate steady long-term income.

Source: Thanachart

COMPANY RATING



Rating Scale

| | |
|------------------|----------|
| Excellent | 5 |
| Good | 4 |
| Fair | 3 |
| Weak | 2 |
| Very Weak | 1 |
| None | 0 |

Source: Thanachart; * CG Rating

THANACHART'S SWOT ANALYSIS

S — Strength

- One of the Big Four contractors in Thailand and categorized as class-A in terms of being qualified to bid for most large-scale investments.
- Business diversification into infrastructure investments to stabilize its long-term earnings.

O — Opportunity

- Thailand is in the middle of the infrastructure investment cycle.
- Its exposure to high-potential projects abroad, especially hydroelectric work in Laos.

W — Weakness

- Most of CK's revenues come from projects it has to bid for, and there are no guarantees it will win these bids.
- CK's interest expenses are high, leading to a significant risk of earnings losses if revenues fall.
- The construction business is labour-intensive, so there are risks of higher labor costs and labor shortages.

T — Threat

- The Covid-19 impacts and the government's time-consuming implementation processes could cause delays to Thailand's infrastructure investment.
- Volatility in building material prices is another risk.

CONSENSUS COMPARISON

| | Consensus | Thanachart | Diff |
|------------------------------|----------------|----------------|----------------|
| Target price (Bt) | 22.63 | 26.00 | 15% |
| Net profit 21F (Bt m) | 878 | 742 | -15% |
| Net profit 22F (Bt m) | 1,462 | 1,099 | -25% |
| Consensus REC | BUY: 17 | HOLD: 0 | SELL: 0 |

HOW ARE WE DIFFERENT FROM THE STREET?

- Our 2021-22F earnings are 15-25% lower than the Bloomberg consensus estimates, which we believe is due to us having a more conservative view on revenue and gross margin.
- However, our SOTP-based TP is 15% higher than other brokers', which we attribute to us having a more bullish view on its associates' business prospects.

Sources: Bloomberg consensus, Thanachart estimates

RISKS TO OUR INVESTMENT CASE

- The key downside risk to our call would be if the government's infrastructure investment projects cannot be implemented, as this would likely prompt us to adjust down our new work value assumptions.
- Building material expenses account for 50-60% of CK's total costs. Therefore, adverse fluctuations in prices present another downside risk to our earnings forecasts.
- The weak economy could have a significant negative impact upon people's confidence and new investments.

Source: Thanachart

INCOME STATEMENT

| FY ending Dec (Bt m) | 2019A | 2020A | 2021F | 2022F | 2023F |
|-----------------------------------|--------------|--------------|--------------|--------------|--------------|
| Sales | 23,189 | 16,941 | 13,842 | 18,722 | 26,611 |
| Cost of sales | 21,028 | 15,341 | 12,661 | 17,124 | 24,340 |
| Gross profit | 2,161 | 1,601 | 1,181 | 1,598 | 2,271 |
| % gross margin | 9.3% | 9.4% | 8.5% | 8.5% | 8.5% |
| Selling & administration expenses | 2,430 | 2,027 | 1,896 | 2,097 | 2,395 |
| Operating profit | (268) | (427) | (715) | (499) | (124) |
| % operating margin | -1.2% | -2.5% | -5.2% | -2.7% | -0.5% |
| Depreciation & amortization | 526 | 726 | 780 | 816 | 852 |
| EBITDA | 258 | 299 | 65 | 317 | 728 |
| % EBITDA margin | 1.1% | 1.8% | 0.5% | 1.7% | 2.7% |
| Non-operating income | 1,560 | 1,226 | 1,190 | 1,141 | 1,065 |
| Non-operating expenses | 0 | 0 | 0 | 0 | 0 |
| Interest expense | (1,226) | (1,276) | (1,291) | (1,290) | (1,323) |
| Pre-tax profit | 65 | (477) | (816) | (648) | (382) |
| Income tax | 126 | 28 | 0 | 0 | 0 |
| After-tax profit | (61) | (505) | (816) | (648) | (382) |
| % net margin | -0.3% | -3.0% | -5.9% | -3.5% | -1.4% |
| Shares in affiliates' Earnings | 1,039 | 857 | 1,571 | 1,764 | 1,821 |
| Minority interests | (15) | (15) | (12) | (16) | (23) |
| Extraordinary items | 815 | 275 | 0 | 0 | 0 |
| NET PROFIT | 1,778 | 612 | 742 | 1,099 | 1,416 |
| Normalized profit | 963 | 337 | 742 | 1,099 | 1,416 |
| EPS (Bt) | 1.0 | 0.4 | 0.4 | 0.6 | 0.8 |
| Normalized EPS (Bt) | 0.6 | 0.2 | 0.4 | 0.6 | 0.8 |

We forecast CK's earnings to recover this year...

...driven by higher earnings contributions from its associates

We also expect a recovery in CK's construction business...

...driving further earnings growth in 2022-23F

BALANCE SHEET

| FY ending Dec (Bt m) | 2019A | 2020A | 2021F | 2022F | 2023F |
|---------------------------------|---------------|---------------|---------------|---------------|---------------|
| ASSETS: | | | | | |
| Current assets: | 18,953 | 19,834 | 17,756 | 21,350 | 26,827 |
| Cash & cash equivalent | 9,160 | 7,767 | 7,500 | 7,500 | 7,500 |
| Account receivables | 3,643 | 3,659 | 3,223 | 4,360 | 6,197 |
| Inventories | 3,751 | 5,757 | 4,856 | 6,568 | 9,002 |
| Others | 2,400 | 2,650 | 2,177 | 2,922 | 4,127 |
| Investments & loans | 51,255 | 50,366 | 47,866 | 45,366 | 42,866 |
| Net fixed assets | 11,164 | 11,194 | 11,214 | 11,197 | 11,145 |
| Other assets | 1,213 | 1,381 | 1,155 | 1,523 | 2,114 |
| Total assets | 82,586 | 82,774 | 77,991 | 79,436 | 82,953 |
| LIABILITIES: | | | | | |
| Current liabilities: | 17,909 | 14,758 | 11,637 | 12,824 | 15,580 |
| Account payables | 13,950 | 10,631 | 7,631 | 8,914 | 11,670 |
| Bank overdraft & ST loans | 1,874 | 147 | 0 | 0 | 0 |
| Current LT debt | 1,525 | 3,670 | 3,667 | 3,523 | 3,356 |
| Others current liabilities | 559 | 309 | 339 | 388 | 555 |
| Total LT debt | 33,605 | 38,586 | 37,078 | 35,620 | 33,932 |
| Others LT liabilities | 3,259 | 3,160 | 2,590 | 3,487 | 4,937 |
| Total liabilities | 54,773 | 56,503 | 51,305 | 51,932 | 54,448 |
| Minority interest | 420 | 424 | 436 | 452 | 476 |
| Preferreds shares | 0 | 0 | 0 | 0 | 0 |
| Paid-up capital | 1,694 | 1,694 | 1,694 | 1,694 | 1,694 |
| Share premium | 4,869 | 4,869 | 4,869 | 4,869 | 4,869 |
| Warrants | 0 | 0 | 0 | 0 | 0 |
| Surplus | 6,341 | 4,572 | 4,572 | 4,572 | 4,572 |
| Retained earnings | 14,488 | 14,711 | 15,115 | 15,917 | 16,893 |
| Shareholders' equity | 27,393 | 25,847 | 26,250 | 27,052 | 28,029 |
| Liabilities & equity | 82,586 | 82,774 | 77,991 | 79,436 | 82,953 |

Sources: Company data, Thanachart estimates

CASH FLOW STATEMENT

| FY ending Dec (Bt m) | 2019A | 2020A | 2021F | 2022F | 2023F |
|-----------------------------------|----------------|----------------|----------------|----------------|----------------|
| Earnings before tax | 65 | (477) | (816) | (648) | (382) |
| Tax paid | (121) | (51) | 5 | (0) | 8 |
| Depreciation & amortization | 526 | 726 | 780 | 816 | 852 |
| Chg In working capital | 2,165 | (5,342) | (1,664) | (1,566) | (1,516) |
| Chg In other CA & CL / minorities | 3,212 | 461 | 2,069 | 1,067 | 776 |
| Cash flow from operations | 5,847 | (4,683) | 375 | (331) | (263) |
| Capex | (1,902) | (756) | (800) | (800) | (800) |
| Right of use | 0 | (121) | (5) | (5) | (5) |
| ST loans & investments | 214 | (8) | 0 | 0 | 0 |
| LT loans & investments | (5,165) | 889 | 2,500 | 2,500 | 2,500 |
| Adj for asset revaluation | 0 | 0 | 0 | 0 | 0 |
| Chg In other assets & liabilities | 730 | 45 | (339) | 534 | 863 |
| Cash flow from investments | (6,124) | 49 | 1,356 | 2,229 | 2,558 |
| Debt financing | 308 | 5,399 | (1,659) | (1,602) | (1,856) |
| Capital increase | 0 | 0 | 0 | 0 | 0 |
| Dividends paid | (847) | (339) | (339) | (297) | (440) |
| Warrants & other surplus | 1,041 | (1,819) | 0 | 0 | 0 |
| Cash flow from financing | 502 | 3,241 | (1,997) | (1,899) | (2,295) |
| Free cash flow | 3,945 | (5,439) | (425) | (1,131) | (1,063) |

VALUATION

| FY ending Dec | 2019A | 2020A | 2021F | 2022F | 2023F |
|-------------------------------------|--------------|--------------|--------------|--------------|--------------|
| Normalized PE (x) | 34.8 | 99.5 | 45.2 | 30.5 | 23.7 |
| Normalized PE - at target price (x) | 45.7 | 130.7 | 59.3 | 40.1 | 31.1 |
| PE (x) | 18.9 | 54.8 | 45.2 | 30.5 | 23.7 |
| PE - at target price (x) | 24.8 | 71.9 | 59.3 | 40.1 | 31.1 |
| EV/EBITDA (x) | 238.1 | 227.7 | 1,022.7 | 205.4 | 86.9 |
| EV/EBITDA - at target price (x) | 278.8 | 262.7 | 1,183.6 | 238.5 | 101.3 |
| P/BV (x) | 1.2 | 1.3 | 1.3 | 1.2 | 1.2 |
| P/BV - at target price (x) | 1.6 | 1.7 | 1.7 | 1.6 | 1.6 |
| P/CFO (x) | 5.7 | (7.2) | 89.5 | (101.4) | (127.7) |
| Price/sales (x) | 1.4 | 2.0 | 2.4 | 1.8 | 1.3 |
| Dividend yield (%) | 2.0 | 1.0 | 0.9 | 1.3 | 1.7 |
| FCF Yield (%) | 11.8 | (16.2) | (1.3) | (3.4) | (3.2) |
| (Bt) | | | | | |
| Normalized EPS | 0.6 | 0.2 | 0.4 | 0.6 | 0.8 |
| EPS | 1.0 | 0.4 | 0.4 | 0.6 | 0.8 |
| DPS | 0.4 | 0.2 | 0.2 | 0.3 | 0.3 |
| BV/share | 16.2 | 15.3 | 15.5 | 16.0 | 16.5 |
| CFO/share | 3.5 | (2.8) | 0.2 | (0.2) | (0.2) |
| FCF/share | 2.3 | (3.2) | (0.3) | (0.7) | (0.6) |

Sources: Company data, Thanachart estimates

*CK now trades 48%
below its associates'
market value...*

*...which we believe is
unjustified*

FINANCIAL RATIOS

| FY ending Dec | 2019A | 2020A | 2021F | 2022F | 2023F |
|----------------------------------|--------|--------|---------|---------|--------|
| Growth Rate | | | | | |
| Sales (%) | (21.4) | (26.9) | (18.3) | 35.3 | 42.1 |
| Net profit (%) | (28.7) | (65.6) | 21.3 | 48.1 | 28.8 |
| EPS (%) | (28.7) | (65.6) | 21.3 | 48.1 | 28.8 |
| Normalized profit (%) | (37.9) | (65.0) | 120.3 | 48.1 | 28.8 |
| Normalized EPS (%) | (37.9) | (65.0) | 120.3 | 48.1 | 28.8 |
| Dividend payout ratio (%) | 38.1 | 55.3 | 40.0 | 40.0 | 40.0 |
| Operating performance | | | | | |
| Gross margin (%) | 9.3 | 9.4 | 8.5 | 8.5 | 8.5 |
| Operating margin (%) | (1.2) | (2.5) | (5.2) | (2.7) | (0.5) |
| EBITDA margin (%) | 1.1 | 1.8 | 0.5 | 1.7 | 2.7 |
| Net margin (%) | (0.3) | (3.0) | (5.9) | (3.5) | (1.4) |
| D/E (incl. minor) (x) | 1.3 | 1.6 | 1.5 | 1.4 | 1.3 |
| Net D/E (incl. minor) (x) | 1.0 | 1.3 | 1.2 | 1.2 | 1.0 |
| Interest coverage - EBIT (x) | na | na | na | na | na |
| Interest coverage - EBITDA (x) | 0.2 | 0.2 | 0.1 | 0.2 | 0.6 |
| ROA - using norm profit (%) | 1.2 | 0.4 | 0.9 | 1.4 | 1.7 |
| ROE - using norm profit (%) | 3.6 | 1.3 | 2.8 | 4.1 | 5.1 |
| DuPont | | | | | |
| ROE - using after tax profit (%) | na | na | na | na | na |
| - asset turnover (x) | 0.3 | 0.2 | 0.2 | 0.2 | 0.3 |
| - operating margin (%) | 5.6 | na | na | na | na |
| - leverage (x) | 3.1 | 3.1 | 3.1 | 3.0 | 2.9 |
| - interest burden (%) | 5.1 | (59.6) | (171.7) | (100.9) | (40.6) |
| - tax burden (%) | na | na | na | na | na |
| WACC (%) | 7.3 | 7.3 | 7.3 | 7.3 | 7.3 |
| ROIC (%) | 0.5 | (0.8) | (0.9) | (0.7) | (0.2) |
| NOPAT (Bt m) | 250 | (427) | (572) | (399) | (99) |
| invested capital (Bt m) | 55,237 | 60,483 | 59,495 | 58,695 | 57,816 |

Sources: Company data, Thanachart estimates

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Thanachart Securities Pcl.

Research Team

19 Floor, MBK Tower

444 Phayathai Road, Pathumwan Road, Bangkok 10330

Tel: 662 - 779-9119

Email: thanachart.res@thanachartsec.co.th

Pimpaka Nichgaroon, CFA

Head of Research

Tel: 662-779-9199

pimpaka.nic@thanachartsec.co.th

Pattarawan Wangmingmat

Senior Technical Analyst

Tel: 662-779-9105

pattarawan.wan@thanachartsec.co.th

Phannarai Tiyapittayarut

Property, Retail

Tel: 662-779-9109

phannarai.von@thanachartsec.co.th

Sarachada Sornsong

Bank, Finance, Insurance

Tel: 662-779-9106

sarachada.sor@thanachartsec.co.th

Sittichet Rungrassameephat

Analyst, Quantitative

Tel: 662-483-8303

sittichet.run@thanachartsec.co.th

Adisak Phupiphathirungul, CFA

Retail Market Strategy

Tel: 662-779-9120

adisak.phu@thanachartsec.co.th

Nuttapop Prasitsuksant

Telecom, Utilities

Tel: 662-483-8296

nuttapop.pra@thanachartsec.co.th

Rata Limsuthiwanoom

Auto, Industrial Estate, Media, Prop. Fund

Tel: 662-483-8297

rata.lim@thanachartsec.co.th

Siriporn Arunothai

Small Cap, Healthcare, Hotel

Tel: 662-779-9113

siriporn.aru@thanachartsec.co.th

Thaloengsak Kucharoenpaisan

Analyst, Retail Market

Tel: 662-483-8304

thaloengsak.kuc@thanachartsec.co.th

Chak Reungsinpinya

Energy, Petrochemical, Paper

Tel: 662-779-9104

chak.reu@thanachartsec.co.th

Pattadol Bunnak

Electronics, Food & Beverage, Shipping

Tel: 662-483-8298

pattadol.bun@thanachartsec.co.th

Saksid Phadthananarak

Construction, Transportation

Tel: 662-779-9112

saksid.pha@thanachartsec.co.th

Witchanan Tambamroong

Technical Analyst

Tel: 662-779-9123

witchanan.tam@thanachartsec.co.th