HLIB Research
PP 9484/12/2012 (031413)

Hektar REIT

Brian Chin Haoyan
brianchy@hlib.hongleong.com.my
+603-2083 1717

HOLD (Initiate)

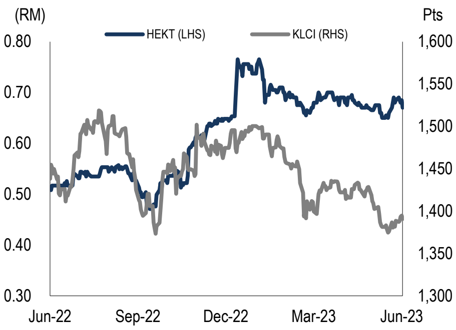
Target Price:	**RM0.60**
Previously:	**N/A**
Current Price:	**RM0.67**

Capital upside	-10.4%
Dividend yield	9.0%
Expected total return	-1.4%

Sector coverage: REIT

Company description: Hektar REIT is a retail-focused REIT invest in real estate in Malaysia, which is primarily used for retail purposes. The Trust's portfolio currently consists of six properties.

Share price



Historical return (%)	1M	3M	12M
Absolute	-4.4	-5.8	17.1
Relative	-0.8	-0.7	30.6

Stock information

Bloomberg ticker	HEKT MK
Bursa code	5121
Issued shares (m)	499
Market capitalisation (RM m)	324
3-mth average volume ('000)	358
SC Shariah compliant	No
F4GBM Index member	Yes
ESG rating	★★★★

Major shareholders

Frasers Centrepoint Trust	28.9%
Hektar Black Sdn Bhd	26.9%

Earnings summary

FYE (Dec)	FY22	FY23f	FY24f
PATMI – core	27.6	30.2	32.7
EPS – core (sen)	5.9	6.4	6.9
P/E (x)	11.4	10.5	9.7

Poised for steady recovery

We initiate coverage on Hektar with a HOLD recommendation and TP of RM0.60, based on FY24f DPU at a targeted yield of 11%. We project Hektar's earnings to grow by 9.5%/8.2%/3.5% for FY23f/FY24f/FY25f – mainly driven by expansion in occupancy rate offsetting the slight negative rental reversion. Our forecasts imply a divvy yield of 9.0%/9.8%/10.1% for the corresponding periods. We opine the stock is commanding a balanced risk to reward profile as its attractive divvy yield should help to alleviate some downside risks arising from the retail space oversupply woes.

Property portfolio… Hektar Real Estate Investment Trust (Hektar) currently owns six retail assets strategically situated across Peninsular Malaysia, namely Subang Parade, Mahkota Parade, Wetex Parade, Central Square, Kulim Central and Segamat Central, with an aggregate asset value of RM1.2bn and a total NLA of 2m sq ft.

…mainly located at secondary towns. Hektar derives the lion's share of revenue (c. 70% in FY22) from towns outside Klang Valley. This, in our view, reduces the cyclical risks typically faced by shopping centres in major cities, due to (i) shoppers in out-of-town shopping centres tend to focus on necessities spending, (ii) less reliance on tourists patronage and (iii) the advantage of little to no competition by being the dominant mall in the particular vicinity.

Portfolio occupancy set to improve. We think Hektar's occupancy level has likely hit its inflection point in end-22 and should gradually improve going forward as local retail sales witnessed encouraging momentum and retailers had turned more comfortable in retaining and expanding its physical presence. However, we highlight bulk of its retail NLA is due for expiry in FY23 (35.5%) and FY24 (27.0%), which may cap upside for its occupancy. That said, Hektar has successfully renewed the 14% of total NLA, setting a positive tone in securing decent renewal rate for the balance 21% NLA expiring in FY23.

Rental reversion outlook. Hektar's rental reversion rate has been in the negative territory for three consecutive years due to rental assistance programmes to retain its tenants during the pandemic while grappling with the increasing competition among mall operators to sustain its occupancy, especially Subang Parade. In our view, Hektar's mild positive rental reversion rate in 1Q23 suggests the negative trend is abating. Nonetheless, we think its overall rental reversion rate would remain slightly negative going forward as it is offering more competitive rental rates in return for better portfolio occupancy.

Gearing profile. Hektar's gearing stood at 44.3% as at 1Q23, which is the highest among our REITs coverage universe. This implies limited debt headroom to perform large acquisition exercise without resorting to cash calls. Should there be any acquisitions on the horizon, we believe there is high possibility of equity dilution setting in unless disposal of assets is on the cards.

Occupancy-driven recovery ahead. We project Hektar's core net profit to grow steadily by 9.5%/8.2%/3.5% in FY23/FY24/FY25, mainly driven by gradual expansion in occupancy rate. Our forecasts imply dividend yield of 9.0%/9.8%/10.1% for the corresponding periods.

Initiate with HOLD, TP: RM0.60. Our TP is based on FY24 DPU on targeted yield of 11.0% – derived from 5-year historical average yield spread between Hektar and MAG10YR. Hektar is set to register decent growth going forward, albeit competition is likely to intensify and cap its near-term upside. Overall, we think the stock is commanding an overall balanced risk to reward profile. Plus, its dividend yield should help cushion its downside risks.

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Dec	FY21	FY22	FY23f	FY24f	FY25f
Cash	60.7	23.2	20.5	24.3	27.1
Investment properties	1164.6	1206.1	1206.1	1206.1	1206.1
Others	5.5	6.3	4.3	4.4	4.5
Total Assets	**1230.7**	**1235.5**	**1230.9**	**1234.8**	**1237.6**
Payables	76.8	57.9	51.8	54.0	55.2
Debt	581.1	551.4	551.4	551.4	551.4
Others	24.9	28.2	28.2	28.2	28.2
Total Liabilities	**682.7**	**637.5**	**631.4**	**633.7**	**634.8**
Unitholders' capital	548.0	598.0	599.5	601.1	602.8
Others	-	-	-	-	-
Equity	**548.0**	**598.0**	**599.5**	**601.1**	**602.8**
Total Liab & Equity	**1230.7**	**1235.5**	**1230.9**	**1234.8**	**1237.6**

Income Statement

FYE Dec	FY21	FY22	FY23f	FY24f	FY25f
Total revenue	96.6	117.4	126.6	132.1	135.6
Prop opex	(49.6)	(58.8)	(65.9)	(69.1)	(70.7)
Net prop income	**47.0**	**58.7**	**60.7**	**63.0**	**64.9**
Other income	0.8	3.4	3.4	3.1	2.5
Net investment income	**47.8**	**62.1**	**64.0**	**66.1**	**67.3**
Mgmt fees	(6.9)	(7.5)	(6.7)	(6.8)	(6.9)
Trustee fees	(0.5)	(0.5)	(0.5)	(0.5)	(0.5)
Other trust exp	(3.0)	(6.3)	(3.4)	(3.4)	(3.4)
Finance costs	(18.7)	(20.2)	(23.3)	(22.8)	(22.8)
Profit before tax	**18.8**	**27.6**	**30.2**	**32.7**	**33.8**
Tax	-	-	-	-	-
Core PAT	**18.8**	**27.6**	**30.2**	**32.7**	**33.8**
EIs	(47.3)	47.0	-	-	-
Reported PAT	**(28.5)**	**74.6**	**30.2**	**32.7**	**33.8**

Cash Flow Statement

FYE Dec	FY21	FY22	FY23f	FY24f	FY25f
Profit before taxation	-31.5	78.0	30.2	32.7	33.8
Interest expense	18.7	20.2	23.3	22.8	22.8
Interest income	-0.7	-1.6	-1.6	-1.3	-0.7
Working capital	13.2	-10.9	-4.1	2.1	1.1
Tax paid	-	-	-	-	-
Others	50.4	-50.4	0.0	0.0	0.0
CFO	**50.0**	**35.4**	**47.8**	**56.3**	**57.0**
Disposal / (purchase)	-	-	-	-	-
Others	0.3	(7.6)	1.6	1.3	0.7
CFI	**0.3**	**-7.6**	**1.6**	**1.3**	**0.7**
Distribution paid	-4.2	-24.6	-28.7	-31.1	-32.1
Borrowings drawdown	30.0	0.0	0.0	0.0	0.0
Borrowings repaid	-30.0	-29.6	0.0	0.0	0.0
Others	-14.4	-20.2	-23.3	-22.8	-22.8
CFF	**-18.6**	**-74.5**	**-52.0**	**-53.8**	**-54.9**
Net CF	**31.7**	**-46.7**	**-2.6**	**3.8**	**2.8**
Beginning Cash	27.3	59.1	23.2	20.5	24.3
Short term funds		10.8			
End Cash	**59.1**	**23.2**	**20.5**	**24.3**	**27.1**

Valuation & Ratios

FYE Dec	FY21	FY22	FY23f	FY24f	FY25f
Core EPU (sen)	2.7	5.9	6.4	6.9	7.1
P/E (x)	24.8	11.4	10.5	9.7	9.4
DPU (sen)	2.5	8.0	6.1	6.6	6.8
Dividend yield	3.8	11.9	9.0	9.8	10.1
Distribution payout ratio	94%	137%	95%	95%	95%
NTA/ unit	1.4	1.3	1.2	1.2	1.3
P/ NTA	0.5	0.5	0.5	0.6	0.5
BVPS (RM)	1.4	1.3	1.2	1.2	1.3
P/B (x)	0.6	0.5	0.5	0.5	0.5
NPI margin	49%	50%	48%	48%	48%
Core PAT margin	19%	24%	24%	25%	25%
ROE	3.4%	4.6%	5.0%	5.4%	5.6%
ROA	1.5%	2.2%	2.5%	2.6%	2.7%
Gearing	47.2%	44.6%	44.8%	44.7%	44.6%
Net gearing	42.3%	42.8%	43.1%	42.7%	42.4%

Key Assumptions

FYE Dec	FY21	FY22	FY23f	FY24f	FY25f
Gross rental income:					
Subang Parade	20.7	23.1	26.4	28.1	28.4
Mahkota Parade	19.1	25.2	27.4	28.0	28.5
Wetex Parade	9.6	11.2	11.8	12.4	12.8
Central Square	6.6	7.3	7.9	8.6	9.1
Kulim Central	9.6	12.3	13.1	13.7	14.2
Segamat Central	2.8	3.4	3.8	3.9	4.1
Total	**68.5**	**82.5**	**90.4**	**94.7**	**97.0**

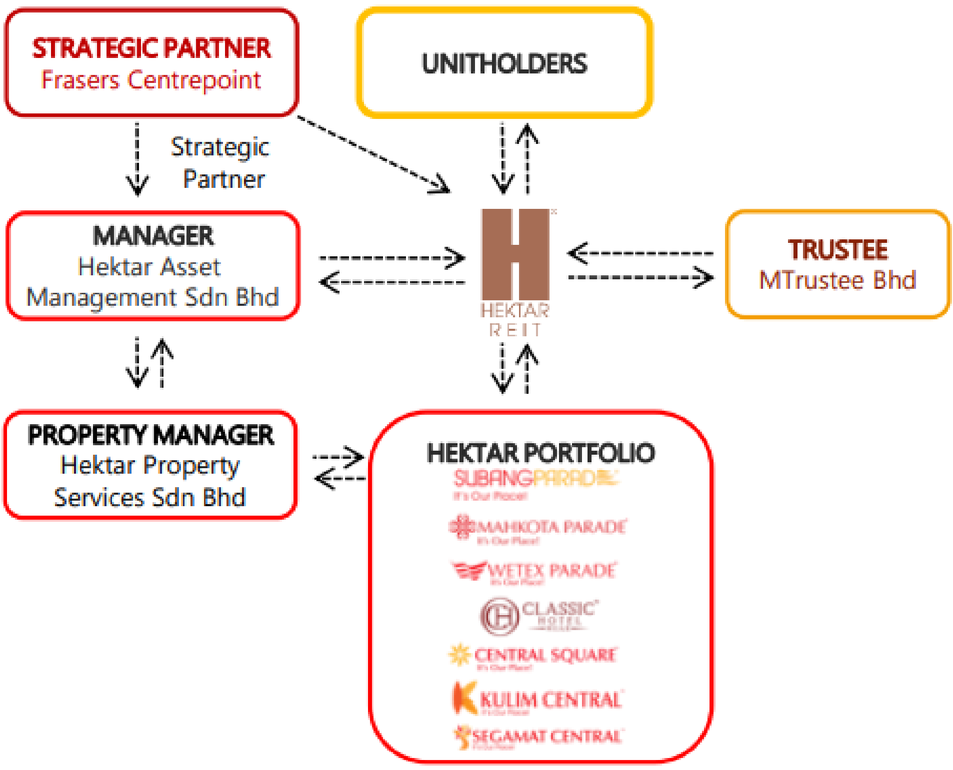
Company Background

Maiden retail-focused REIT in Bursa Malaysia. Listed on 4 December 2006 as the first retail focused Real Estate Investment Trust (REIT) on the Main Board of Bursa Malaysia, Hektar Real Estate Investment Trust ("Hektar") holds a portfolio of retail properties strategically situated across Peninsular Malaysia. Hektar currently owns six retail assets, namely Subang Parade, Mahkota Parade, Wetex Parade, Central Square, Kulim Central and Segamat Central with an aggregate value of RM1.2bn. In sum, Hektar commands a total NLA of 2m sq ft with more than 350 tenants across its portfolio.

REIT Manager. Hektar is managed by Hektar Asset Management Sdn Bhd (Manager) which was formed with a vision to set strategic directions in managing the REIT's assets and liabilities and make recommendations on potential acquisitions, investments and enhancements of assets under management. As required by the Capital Markets and Services Act 2007, the Manager holds a valid Capital Markets Services License (CMSL) issued by the Securities Commission.

Strategic partner: Frasers Centrepoint Trust. Since the acquisition of 27% stake in Hektar REIT in 2007 and subsequently raising it to 31% in 2008, the Frasers Centrepoint Trust (FCT) is the strategic partner of Hektar REIT. Listed on the SGX, FCT is one of the largest owners of suburban retail centres, which consist of nine retail malls and an office building with approximately 2.2m sq ft of net lettable area (NLA). FCT is sponsored by Frasers Centrepoint Limited (FCL). Notably, FCL is a leading company with a strong foothold in property development, property investment and serviced residences. It is also the real estate arm of Fraser & Neave, Limited. The strategic alliance enables both parties to leverage on respective domain expertise and experiences in the retail industry as well as collaborate on joint venture opportunities and obtaining financial support.

Figure #1 **Hektar's corporate structure**



Company

Figure #2 Key milestones

Year	Key milestones
2006	▪ Listed on the Main Board of Bursa Malaysia Securities Berhad on 4 Dec 2006 as Malaysia's first retail-focused REIT with portfolio valued at RM512m.
2007	▪ Announced Cornerstone Investment by FCT via an acquisition of 27% stake in Hektar.
2008	▪ Signing of Joint-Venture Agreement with FCL ▪ FCL Acquired 40% of Hektar Asset Management (REIT manager) and jointly manage Hektar ▪ FCT raised holdings in Hektar to 31% ▪ Completed the acquisition of Wetex Parade & Classic Hotel for RM117.5m
2010	▪ Mahkota Parade celebrated a relaunch after an extensive RM30.4m refurbishment
2012	▪ Acquired Landmark Central Shopping Centre and Central for RM181m
2015	▪ Acquired Segamat Sentral (previously known as 1Segamat Mall)
2018	▪ Won Gold at Asia Pacific Best of the Breeds REITs Awards under 'Retail REIT' category ▪ Won the "Green Initiative Award" at the Asia Corporate Excellence & Sustainability Awards 2019
2019	▪ Honoured at the National Energy Awards 2019 in the Energy Efficient Building – Retrofitted Building category

Company, HLIB Research

Figure #3 Hektar's properties

	Subang Parade	Mahkota Parade	Wetex Parade	Central Square	Kulim Central	Segamat Central
State	Selangor	Melaka	Johor	Kedah	Kedah	Johor
Title	Freehold	Leasehold (Expiry: 2101)	Freehold	Freehold	Freehold	Leasehold (Expiry: 2116)
NLA (sq ft)	527,139	521,142	174,651	310,564	299,781	211,919
Acquisition price	RM280.0m	RM232.0m	RM117.5m	RM83.0m	RM98m	RM104.0m
Valuation	RM417.0m	RM338.5m	RM156.6m	RM91.0m	RM138.0m	RM65.0m
Year opened	1988	1994	1996	1997	2009	2011
Year acquired	2006	2006	2008	2012	2012	2017

Company, HLIB Research

Management team

Figure #4 Key management personnel

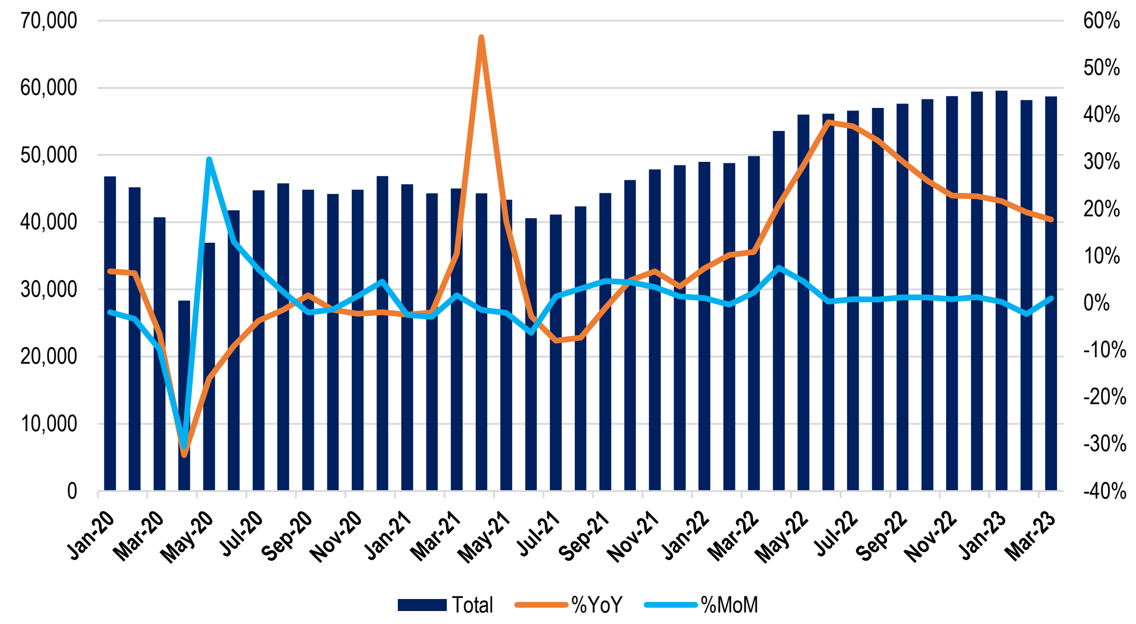
Name	Position	Details
Johari Shukri bin Jamil	Chief Executive Officer	▪ Held various senior management positions in Johor Corporation (JCorp), EA Technique, Iskandar Investment Bhd, JCorp, among others.
Zarina Halim	Chief Corporate Officer	▪ >20 years of experience with the Hektar Group, having been part of the founding team and responsible for the listing of Hektar. ▪ Vast experience in project management and business development
Sabrina Halim	GM, Business Development & Strategy	▪ Joined Hektar in 2010 and has headed various departments ▪ Contributed to the concept and planning for several retail projects, including revamping and expansion exercises
Lim Kek Siang	Senior General Manager, Finance	▪ >26 years of extensive experience in accounting, corporate taxation, financial reporting and corporate finance. ▪ Previously attached to several public listed entities and advised on project-financing arrangements, structured corporate debts and M&A activities.
Martin Chen	General Manager , Legal	▪ >15 years of experience with the group ▪ Extensive experience in legal practice with various law firms ▪ An Advocate and Solicitor, Registered Property Manager by BOVEAP and a holder of CMSRL by the SC of Malaysia

Company, HLIB Research

Industry Overview

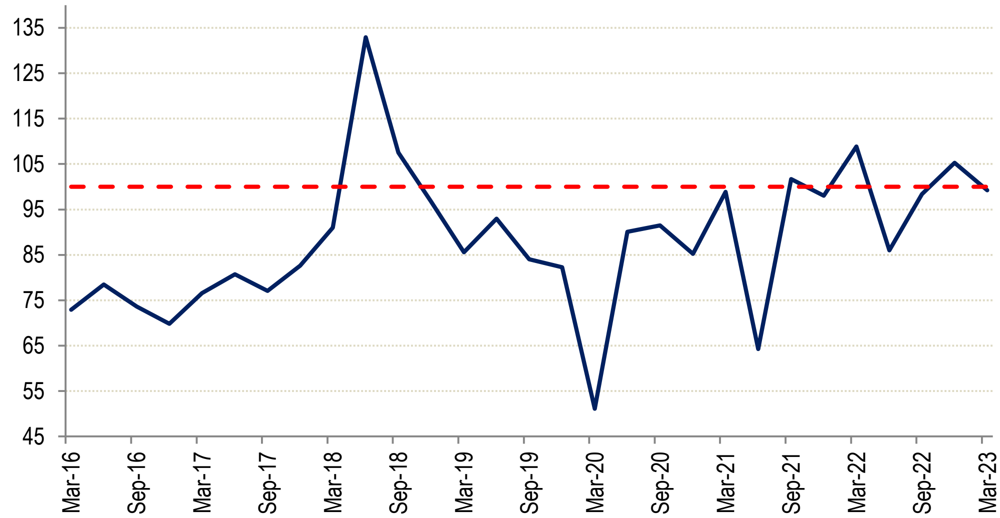
Remarkable recovery in retail industry since endemic… Battered by the Covid-19 pandemic, the retail industry sales showed weaknesses in 2020 and 2021 as most retailers experienced intermittent closures due to the imposition of movement restrictions across the nation. As Malaysia entered endemicity in April 2022 – which entails no limitations on operating hours and capacity constraints of commercial and restaurant premises – retail sales roared back in 2022 with no signs of meaningful pullback yet. The impressive recovery was also aided by festive driven consumption and revenge spending, which saw consumers eager to go out and spend after having been cooped up in their homes for almost two years. We believe the performance of the retail sector would stabilise moving forward as Retail Group Malaysia is forecasting a modest 4.0% YoY growth in retail sales in 2023. Although the rising costs of living and OPR hikes over the past year is expected to dampen household consumption, we think the retail sector would remain resilient on the back of higher tourists arrival in Malaysia. Also, the return of Chinese patronage is set to support retail performance and alleviate the negative spill overs stemming from economic slowdown from the West.

Figure #5 **DOSM retail sales trend**



DOSM, HLIB Research

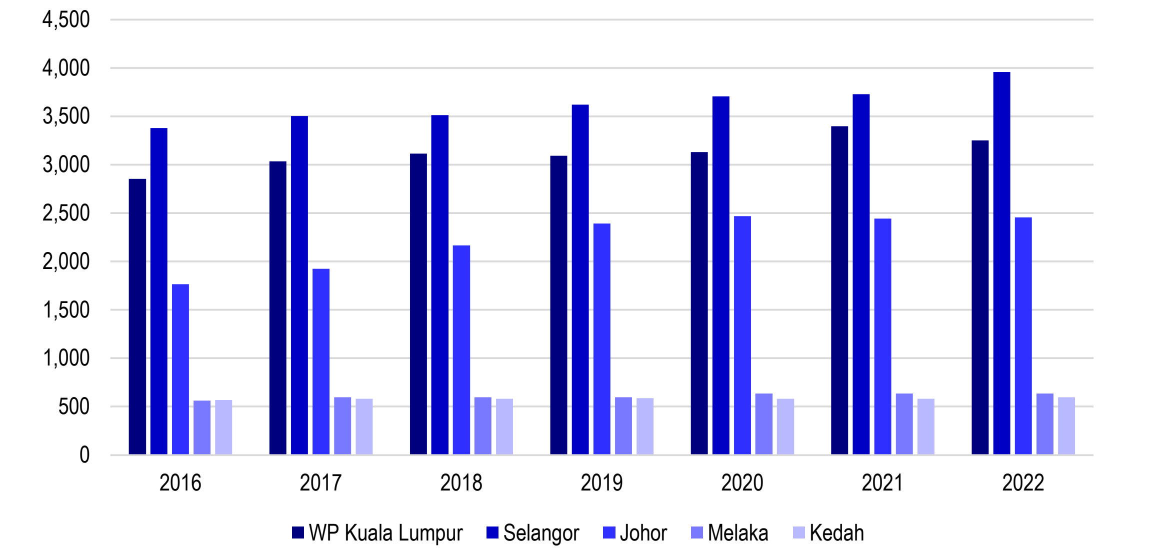
Figure #6 **MIER consumer sentiment index**



MIER, HLIB Research

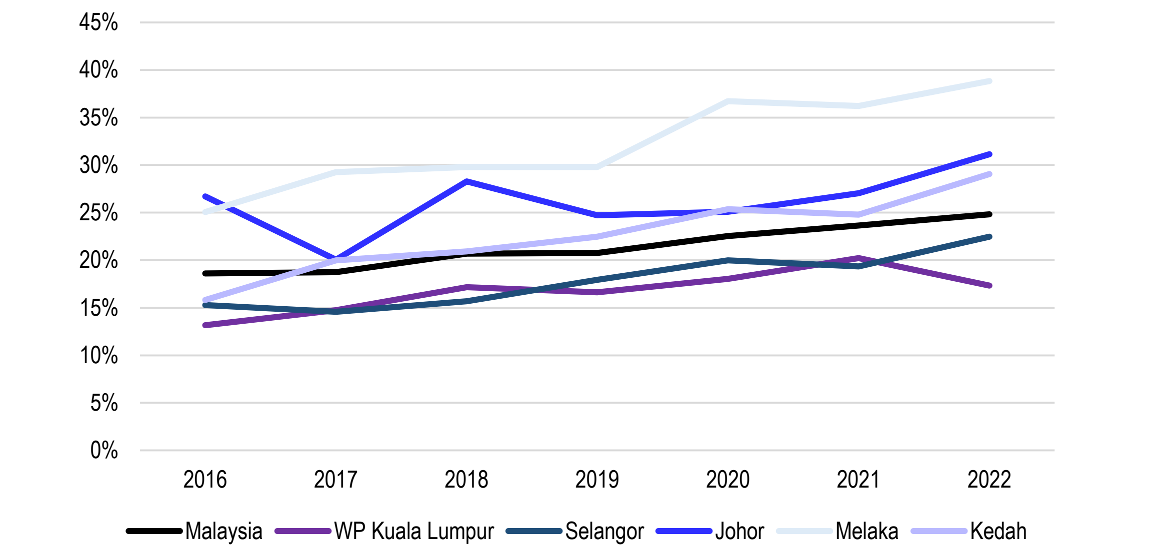
…balanced off by persistent overhang of retail spaces. Despite the sustained growth in retail sales (barring pandemic years), the vacancy rate of shopping complexes in Malaysia has been on the rise over the past years (currently stands at c. 25%). The up-trending vacancy rates was mainly driven by mushrooming supplies of retail space mainly due to the completion of new shopping malls (especially from primary cities in Kuala Lumpur, Selangor and Johor). Although retail space supplies of Melaka has stagnated over the years, the state registered a whopping 39% vacancy rate. In our view, the predicament was attributable to (i) expansion of commercial developments over the past decade (retail space CAGR growth of 6.4% from 363k sm in 2013 to 635.4k sm in 2022) and (ii) its reliance on tourists to support economic activities was rearing its ugly head when the pandemic struck – tourism under the services sector recorded as the most important economic sector in the state, accounting almost half of its GDP during pre-Covid era (Syakir Amir et al.). Overall, we think the incoming supply of retail space (esp. Klang Valley) in the pipeline may continue to intensify competition and suppress industry occupancy rate, thus weigh on the industry rental upside. The negative impact stemming from the heightened vacancy rates in Malaysia varies across shopping malls, depending on locations, options available for shoppers that reside in the catchment area, tenancy mix strategy as well as track record of the shopping malls' brand. In other words, not all malls are created equal. Taking cue from their robust occupancy level (>90%) and consistent positive rental reversion, prime shopping malls in Klang Valley (i.e. Pavilion KL, Sunway Pyramid, Midvalley Megamall) are largely unscathed by the oversupply woes, leveraging on their strategic location, strong brand name and well-strategized tenancy mix that appeals to shoppers with growing discretionary spending power. Meanwhile, less established malls in Klang Valley are struggling to garner footfall and facing dwindling occupancy and rental rates due to limited bargaining power as retailers opt for cheaper options and higher traffic areas.

Figure #7 **Total existing space of shopping complex ('000 s.m)**



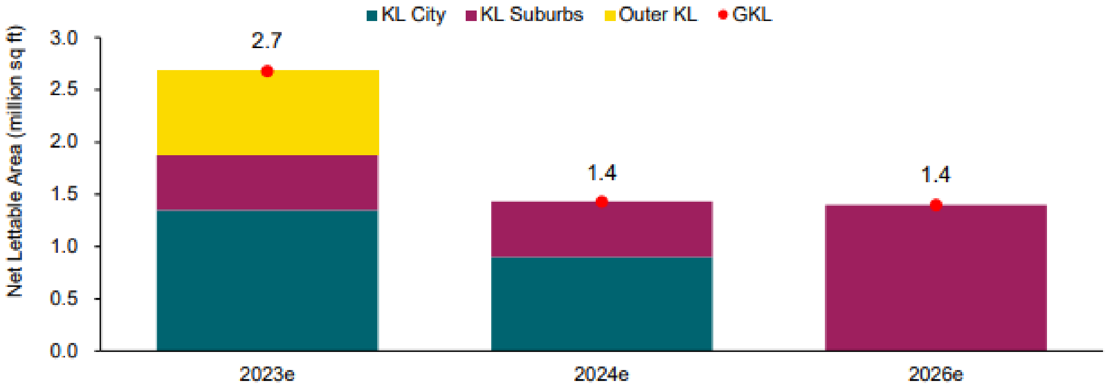
NAPIC, HLIB Research

Figure #8 **Vacancy rate of shopping complex (%)**



NAPIC, HLIB Research

Figure #9 Greater KL's retail space supply pipeline by region (%)

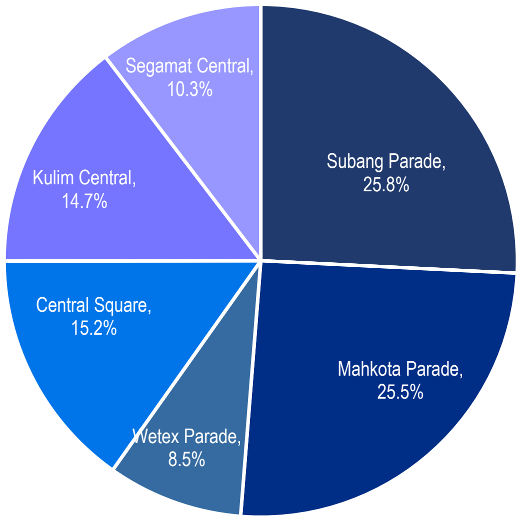


Savills Research

Key Highlights

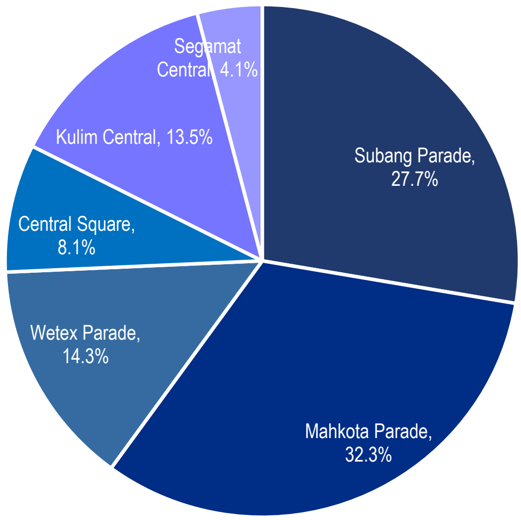
Geographically diversified neighbourhood malls… In contrast with most retail REITs on the local bourse (i.e. Sunway REIT, Pavilion REIT, IGB REIT) which mostly operate regional shopping malls in major cities like Klang Valley, Hektar has a geographically diversified portfolio with its presence in neighbourhood malls scattered across Peninsular Malaysia. Save for Subang Parade, shopping malls under its umbrella are operating in secondary towns situated in Johor, Kedah and Melaka. In fact, about three quarters of its total NLA are located outside Klang Valley. Furthermore, unlike regional shopping malls that mainly focus on one-stop shopping and leisure as well as discretionary spending, Hektar positions its assets as neighbourhood shopping centres that are skewed towards necessities spending. To note, regional malls usually command a sheer NLA ranging from 500k to 2m sqft as compared <500k sqft for neighbourhood malls.

Figure #10 NLA (sq ft) breakdown by assets



Company, HLIB Research

Figure #11 Gross revenue breakdown by assets (FY22)

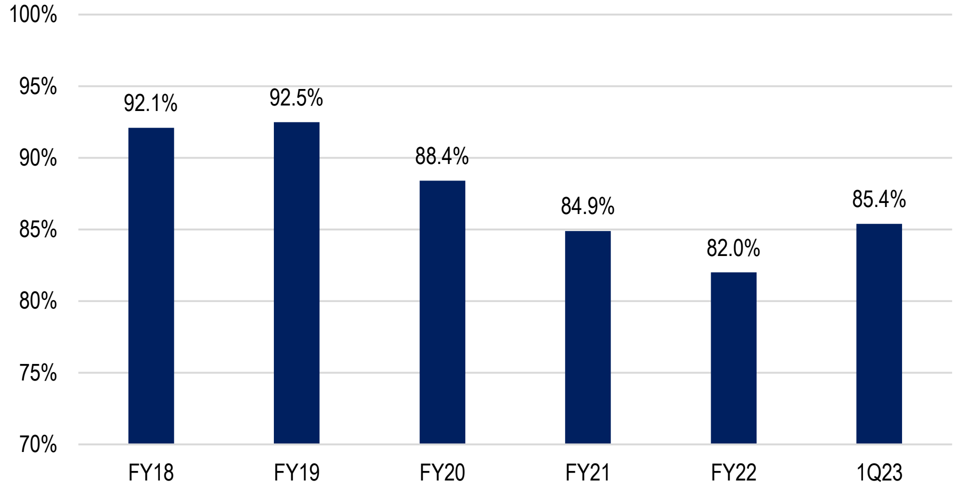


Company, HLIB Research

…helps to alleviate concentration risk. Hektar's diversified portfolio helps alleviate its geographical concentration risk. As opposed to having most of its malls in prime city areas like its peers, Hektar derives its lion's share of revenue (c. 70% in FY22) from towns outside Klang Valley. This, in our view, reduces the cyclical risks typically faced by prime shopping centres. Case in point, the former CEO of Hektar, Datuk Hisham Othman shared with The Edge that the impact on footfall at the out-of-town malls was not as severe in Klang Valley during the Covid pandemic, thanks to the following factors: (i) shoppers of out-of-town shopping centres tend to focus on necessities spending, (ii) less reliance on tourists patronage (except Mahkota Parade in Melaka) and (iii) the advantage of little to no competition by being the dominant mall in the particular vicinity, especially for Wetex Parade, Kulim Central, Central Square and Segamat Central. Although Melaka is struggling with overhang of retail space (nearly 40% vacancy rate), Mahkota Parade being one of the main shopping destinations in the state has remained resilient with nearly 90% occupancy rate, flexing its strong appeal to both tenants and shoppers.

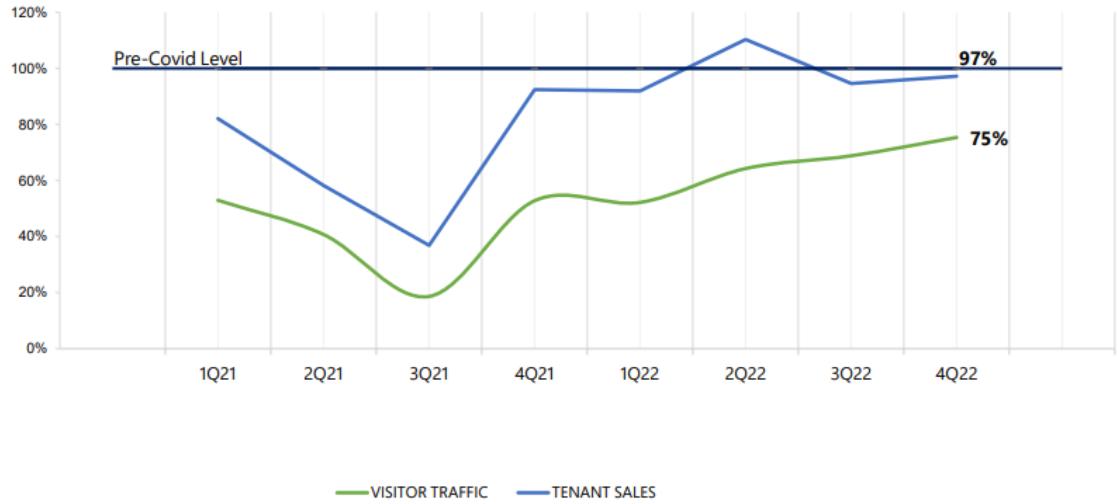
Portfolio occupancy has likely bottomed out… Hektar saw an apparent decline in its overall occupancy level from FY20-22 (see figure#12) as many retailers were struggling to stay afloat during the pandemic era and hence, opted to shut their doors. The occupancy slump was largely contributed by Subang Parade and Mahkota Parade which were operating in larger cities. Meanwhile, the rest of its malls in secondary towns remained fairly stable, thus aiding in cushioning the overall decline in occupancy. This could be explained by, in our view, the non-discretionary nature shopper base of its neighbourhood malls in secondary towns alongside its minimal exposure to tourist footfall as explained above. As more shoppers set foot to its malls and with tenancy sales returning to pre-pandemic level in 2022, its portfolio occupancy hit an inflection point by end of FY22 and improved to 85% in early-FY23. We think its occupancy level has likely hit its bottom in FY22 and should gradually improve going forward as local retail sales witnessed encouraging momentum while retailers had turned more comfortable in retaining and expanding their brick-and-mortar presence.

Figure #12 Overall portfolio occupancy



Company, HLIB Research

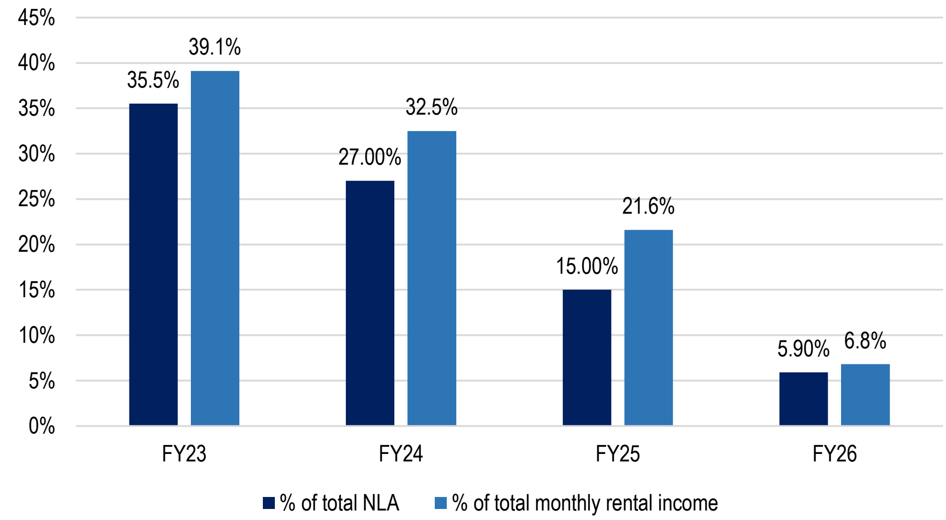
Figure #13 Portfolio footfall & tenant sales vs Pre-Covid level (2019)



Company

…but non-renewal risks may cap occupancy upside. While we are positive on the retail industry outlook coupled with Hektar's recovering portfolio occupancy thus far, we highlight bulk of its retail NLA is due for expiry in FY23 (35.5%) and FY24 (27.0%) (see figure #14). In our view, these may cap upside for its overall occupancy should Hektar fail to extend most of its leases due for expiry with its existing tenants. As at 1Q23, Hektar has successfully renewed the leases with 78 tenants covering 14% of total NLA, setting a positive tone in securing decent renewal rate for the balance 21% NLA due for expiry for FY23. We also take comfort in management's optimistic tone with the aim of renewing the entire expiring NLA this year.

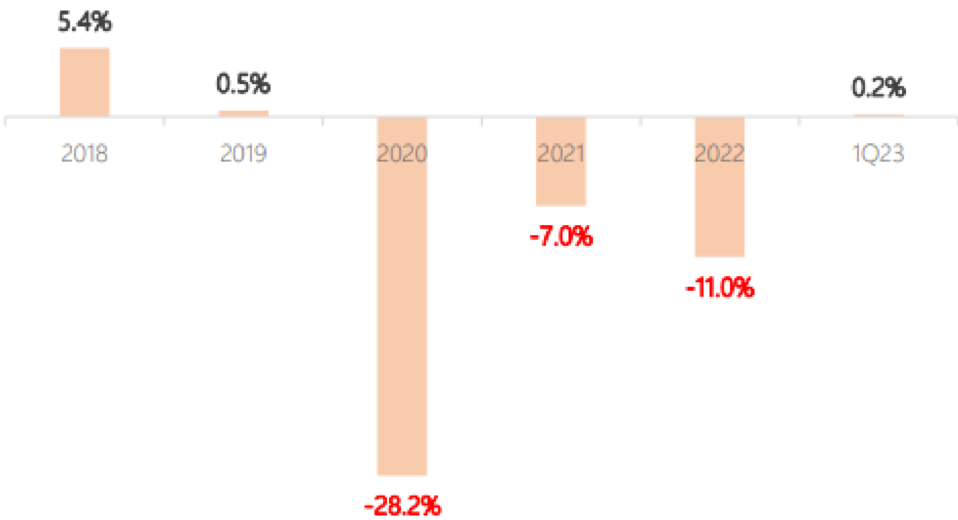
Figure #14 Portfolio tenancy expiry profile



Company, HLIB Research

Rental reversion outlook. Referring to figure#15, Hektar's rental reversion rate has been in the negative territory for three consecutive years since the outbreak of Covid-19 due to rental assistance programmes to retain its tenants while grappling with the increasing competition among shopping malls to sustain occupancy. Hektar's mild positive rental reversion rate in 1Q23 (mainly driven by rental rate expansion in Mahkota Parade and Kulim Central offsetting the decline in Subang Parade, Wetex Parade and Central Square) suggests the negative rental reversal trend could be abating. We still believe FY23 overall rental reversion rate would stay slightly negative as our checks indicate that Hektar is offering more competitive rental rates for its underperforming malls (especially Subang Parade given the intense competition) in return for better portfolio occupancy. This strategy is premised on the notion that a marginal drop in rental rates should be sufficiently offset by the enhancement in occupancy level, thus positively contributing to its revenue stream on a net basis.

Figure #15 Hektar's 5-year rental reversion trend



Company

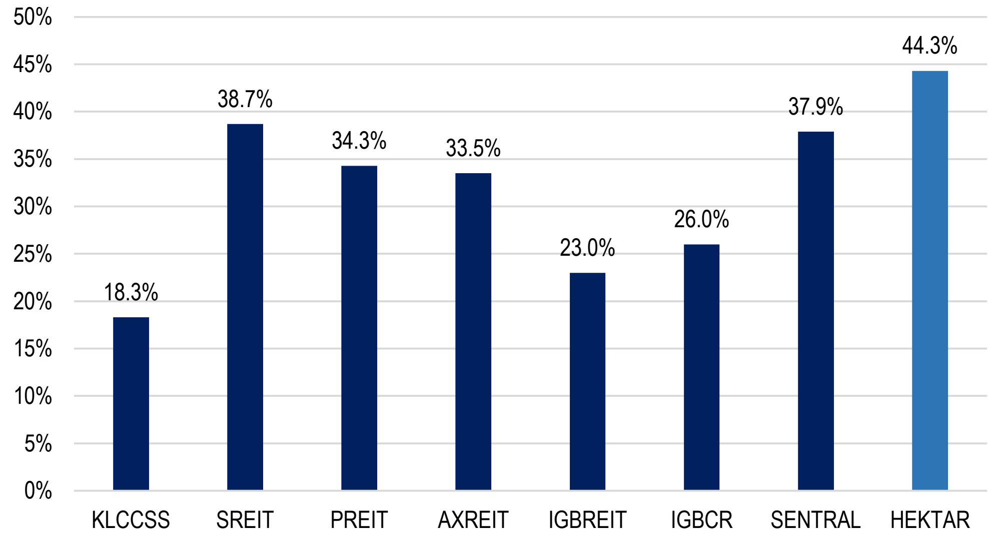
Figure #16 FY22 rental reversions breakdown by assets

	Number of new tenancies/renewals	NLA (sqft)	% of total NLA	% change over previous rent rates
Subang Parade	33	69,930	13.2%	-4.9%
Mahkota Parade	55	174,979	33.6%	-13.5%
Wetex Parade	26	23,185	13.3%	-7.9%
Central Square	12	44,556	14.3%	-4.2%
Kulim Central	21	35,378	11.8%	22.0%
Segamat Central	31	118,869	56.1%	-35.0%
Total/Average*	**178**	**466,357**	**22.8%***	**-11.0%**

Company, HLIB Research

Gearing profile. Similar with other REITs listed on Bursa, Hektar is bounded by the SC's Guidelines on Listed Real Estate Investment Trusts (REITs), of maintaining its gearing level below 50%. Hektar's indebtedness stood at 44.3% as at 1Q23, which is the highest among our REITs coverage universe (see figure#17). Assuming gearing up to the permissible limit, Hektar would only be able to drawdown circa RM140m borrowings to undertake asset acquisitions (as asset value increases with debt load) based on our estimates. The amount only accounted for about 9% of Hektar's total assets, implying limited debt headroom to perform large acquisition exercise without resorting to cash calls. Should there be any acquisitions on the horizon, we believe there is high possibility of equity dilution setting in unless disposal of assets is on the cards.

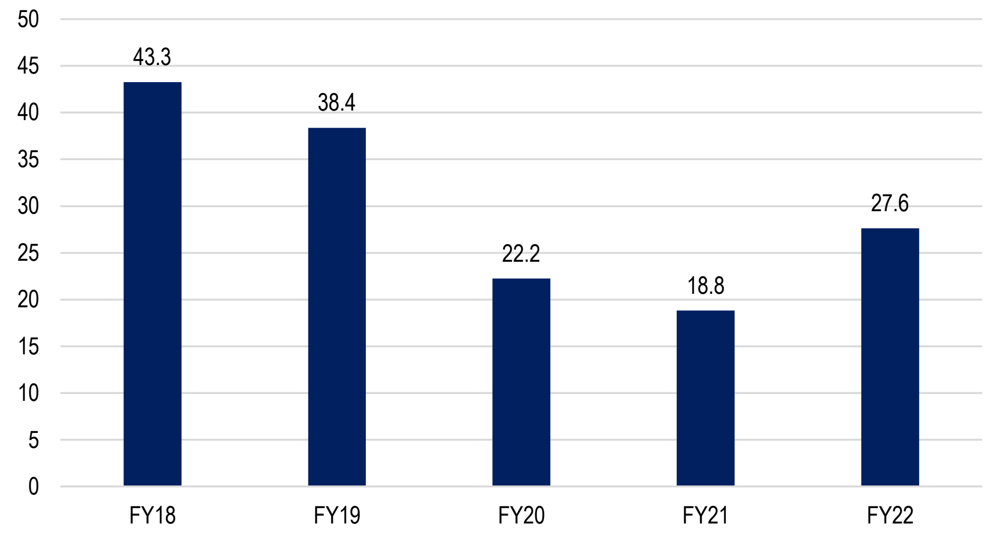
Figure #17 **Gearing profile of our coverage universe as at 1QCY23**



Companies, HLIB Research

Financial Overview

Figure #18 **Historical financial review – core net profit (RM' m)**



Company, HLIB Research

Earnings hit by Covid-19 pandemic and intense competition. Impacted by the Covid-19 pandemic and intense competition among retail malls, Hektar saw down-trending bottom line during FY18-21, mirroring the negative trend of rental rates and portfolio occupancy as outlined earlier. Nonetheless, Hektar saw light at the end of the tunnel as the nation entered into endemicity in early 2022. As tenancy sales rebounded back to pre-pandemic levels alongside a significant reduction in rental assistance, Hektar staged a decent recovery in FY22.

Figure #19 Latest quarterly result summary

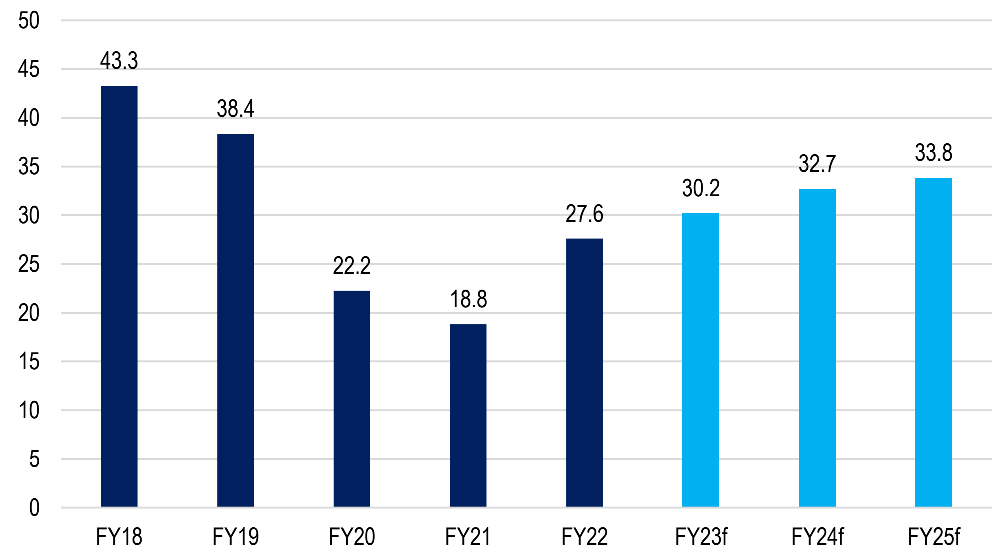
	1Q22	4Q22	1Q23	QoQ (%)	YoY (%)
Total revenue	**29.1**	**27.9**	**28.9**	**3.8%**	**-0.6%**
Total property opex	-12.5	-17.8	-13.7	-23.1%	9.9%
Net property income	**16.6**	**10.0**	**15.2**	51.5%	-8.5%
Interest income	0.1	1.3	0.0	-98.8%	-76.9%
Other income	1.6	-0.6	0.6	N.A.	-59.3%
Trust expenses	-2.4	-2.4	-2.5	5.6%	4.5%
Finance expenses	-4.4	-5.9	-6.2	6.0%	42.8%
Core PBT	**11.5**	**2.6**	**7.1**	**177.5%**	**-37.9%**
Taxation	0.0	0.0	0.0	N.A.	N.A.
Core PAT	**11.5**	**2.6**	**7.1**	**177.5%**	**-37.9%**
Core EPU (sen)	2.4	0.5	1.5	175.8%	-38.3%
DPU (sen)	0.0	5.3	0.0	N.A.	N.A.

Company, HLIB Research

QoQ. Hektar's 1Q23 revenue merely rose 3.8% but NPI grew at a much faster clip (+51.5%) due to lower property opex (-23.1%) as higher upkeep, repair and maintenance costs were incurred in the preceding quarter. As a result, core net profit rose 1.8x relative to 4Q22, coming from a low base.

YoY. Although revenue stayed flattish (-0.6%), Hektar's core net profit in 1Q23 dropped 37.9% due to (i) higher property opex (+9.9%; stemming from higher utilities expenses as a result of electricity tariff hike) and (ii) increased financed expenses (+42.8%; lifted by past interest rate hikes).

Figure #20 Core net profit (RM' m) forecasts

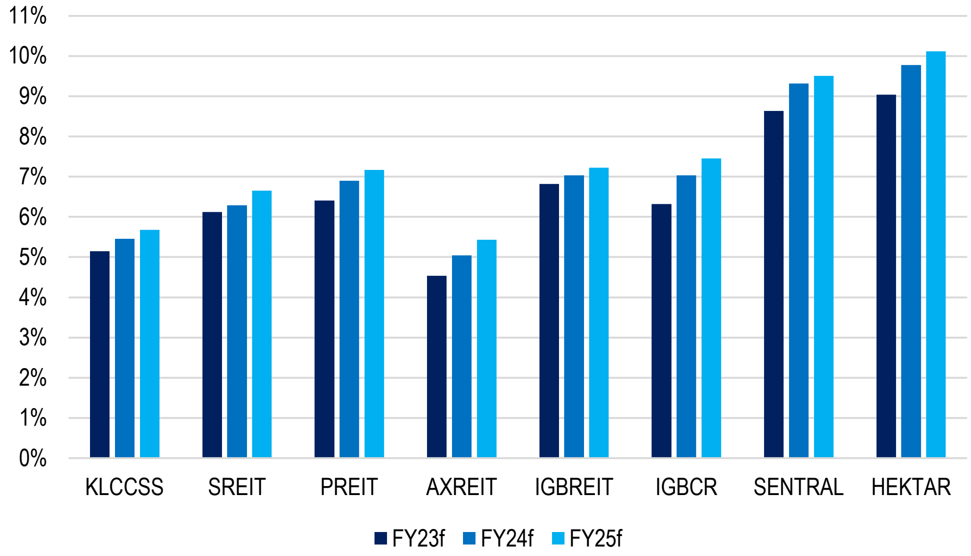


HLIB Research

Poised for gradual recovery. We project Hektar's core net profit to grow steadily by 9.5%/8.2%/3.5% to RM30.2m/RM32.7m/RM33.8m, respectively in FY23f/FY24f/FY25f. Earnings growth for the corresponding periods will be mainly driven by gradual expansion in occupancy rate, albeit with slightly negative rental reversion rate, in line with Hektar's ongoing strategy to stay competitive in attracting and retaining tenants.

Attractive dividend yield. Assuming a distribution ratio of 95% for Hektar, our forecasts translates to DPU of 6.1sen/6.6sen/6.8sen for FY23f/FY24f/FY25f, which implies an attractive dividend yield of 9.0%/9.8%/10.1%, respectively based on the closing price of at 2-Jun-23. When stacked against its peers in our REITs coverage universe, Hektar offers the most generous dividend yield based on our in-house projections.

Figure #21 **Hektar's FY23f-25f dividend yield**



Bloomberg, HLIB Research

Valuation & Recommendation

Initiate with HOLD, TP: RM0.60. We initiate coverage on Hektar with a **HOLD** rating and TP of **RM0.60**. Our TP is based on FY24 DPU on targeted yield of 11.0% – derived from 5-year historical average yield spread between Hektar and MAG10YR. Hektar had suffered major hardship through the pandemic years but we believe the worst is in the rear view mirror as it is set to deliver decent growth going forward, capitalising on the broad revival of retail spending. But on the other hand, we note that the competition among shopping malls is likely to intensify in the near-to-mid term given the growing pipeline of retail malls coming into the market which would exacerbate oversupply woes. These, in our view, may cap its occupancy and rental upside, particularly its assets in Klang Valley and Melaka. Given that the stock has risen about 30% to its current level (relative to last year same period at c. RM0.50), it has likely priced in the recovery prospects of Hektar. Hence, we think the stock is commanding an overall balanced risk to reward profile. Meanwhile, its attractive dividend yield should help to alleviate some downside risks. Re-rating catalysts, in our view, include (i) better-than-expected occupancy and rental momentum and (ii) acquisition of yield accretive assets.

Figure#22 Peer comparison

Stock	Mkt Cap (RM m)	Price (RM)	Target (RM)	Rating	FYE	P/E (x)		P/B (x)		Yield (%)	
						FY23	FY24	FY23	FY24	FY23	FY24
Al-'Aqar Healthcare REIT	1,058	1.26			Dec	14.3	14.7	NA	NA	6.3%	6.2%
Al-Salam REIT	270	0.47			Mar	16.0	12.2	NA	NA	5.2%	6.9%
AmanahRaya REIT	272	0.48			Dec	NA	NA	NA	NA	NA	NA
AME REIT	642	1.23		RESTRICTED	Mar	NA	NA	NA	NA	NA	NA
AmFIRST REIT	227	0.33			Mar	NA	NA	NA	NA	NA	NA
Atrium REIT	369	1.39			Dec	NA	NA	NA	NA	NA	NA
Axis REIT	3,186	1.83	2.16	BUY	Dec	21.7	19.5	1.2	1.1	4.5%	5.0%
CLMT	1,376	0.51			Dec	12.8	11.6	0.4	0.5	8.6%	9.4%
Hektar REIT	334	0.67	0.60	HOLD	Dec	10.5	9.7	0.5	0.5	9.0%	9.8%
IGB REIT	5,859	1.63	1.88	BUY	Dec	16.2	15.7	1.5	1.5	6.8%	7.0%
IGBCR	1,186	0.51	0.51	HOLD	Dec	16.0	14.4	0.5	0.5	6.3%	7.0%
KIP REIT	546	0.90			Jun	13.0	11.5	NA	NA	6.9%	7.8%
KLCCSS	12,421	6.88	6.68	HOLD	Dec	18.0	17.3	0.8	0.8	5.2%	5.5%
Pavilion REIT	4,415	1.21	1.62	BUY	Dec	14.3	13.3	0.9	0.9	6.7%	7.2%
Sentral REIT	884	0.83	0.81	HOLD	Dec	11.6	10.7	0.7	0.7	8.6%	9.3%
Sunway REIT	5,377	1.57	1.87	BUY	Dec	15.6	15.0	1.0	1.0	6.2%	6.3%
Tower REIT	116	0.42			Dec	NA	NA	NA	NA	NA	NA
UOA REIT	757	1.12			Dec	11.5	11.3	0.8	0.8	8.5%	8.8%
YTL Hosp REIT	1,611	0.95			Jun	11.3	10.2	NA	NA	8.5%	10.1%
Average						**14.5**	**13.4**	**0.8**	**0.8**	**7.0%**	**7.6%**

Bloomberg, HLIB Research

Disclaimer

The information contained in this report is based on data obtained from sources believed to be reliable. However, the data and/or sources have not been independently verified and as such, no representation, express or implied, are made as to the accuracy, adequacy, completeness or reliability of the info or opinions in the report.

Accordingly, neither Hong Leong Investment Bank Berhad nor any of its related companies and associates nor person connected to it accept any liability whatsoever for any direct, indirect or consequential losses (including loss of profits) or damages that may arise from the use or reliance on the info or opinions in this publication.

Any information, opinions or recommendations contained herein are subject to change at any time without prior notice. Hong Leong Investment Bank Berhad has no obligation to update its opinion or the information in this report.

Investors are advised to make their own independent evaluation of the info contained in this report and seek independent financial, legal or other advice regarding the appropriateness of investing in any securities or the investment strategies discussed or recommended in this report. Nothing in this report constitutes investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate to your individual circumstances or otherwise represents a personal recommendation to you.

Under no circumstances should this report be considered as an offer to sell or a solicitation of any offer to buy any securities referred to herein.

Hong Leong Investment Bank Berhad and its related companies, their associates, directors, connected parties and/or employees may, from time to time, own, have positions or be materially interested in any securities mentioned herein or any securities related thereto, and may further act as market maker or have assumed underwriting commitment or deal with such securities and provide advisory, investment or other services for or do business with any companies or entities mentioned in this report. In reviewing the report, investors should be aware that any or all of the foregoing among other things, may give rise to real or potential conflict of interests.

This report may provide the addresses of, or contain hyperlinks to websites. Hong Leong Investment Bank Berhad takes no responsibility for the content contained therein. Such addresses or hyperlinks (including addresses or hyperlinks to Hong Leong Investment Bank Berhad own website material) are provided solely for your convenience. The information and the content of the linked site do not in any way form part of this report. Accessing such website or following such link through the report or Hong Leong Investment Bank Berhad website shall be at your own risk.

1. As of 26 June 2023, Hong Leong Investment Bank Berhad has proprietary interest in the following securities covered in this report:
(a) -.

2. As of 26 June 2023, the analyst(s) whose name(s) appears on the front page, who prepared this report, has interest in the following securities covered in this report:
(a) -.

Published & printed by:

Hong Leong Investment Bank Berhad (10209-W)
Level 28, Menara Hong Leong,
No. 6, Jalan Damanlela,
Bukit Damansara,
50490 Kuala Lumpur
Tel: (603) 2083 1800
Fax: (603) 2083 1766

Stock rating guidelines

BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% over the next 12 months.
SELL	Expected absolute return of -10% or less over the next 12 months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result to a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating guidelines

OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next 12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

The stock rating guidelines as stipulated above serves as a guiding principle to stock ratings. However, apart from the abovementioned quantitative definitions, other qualitative measures and situational aspects will also be considered when arriving at the final stock rating. Stock rating may also be affected by the market capitalisation of the individual stock under review.