Asia Credit Research

Heeton Holdings Ltd: Credit Update

Wednesday, 28 February 2018

Growing in Singapore and abroad

- Following the completion of OCBC's engagement, we resume coverage on Heeton Holdings Ltd ("HHL") with an **Issuer Profile of Neutral (5)**.
- Having completed Onze@Tanjong Pagar in Jan 2017, HHL has entered into partnerships to develop more properties in Singapore. In addition, HHL has 8 hotels in the portfolio, with 3 more in the pipeline.
- While HHL has not stated the use of proceeds for the SGD118mn bond issuance, we believe it may be a continuation of its expansion plans in Singapore and abroad. Assuming that the bond proceeds will be fully consumed, we expect that net gearing will rise to ~0.8x (4Q2017: 0.65x). Given HHL's manageable credit profile, backed by assets and recurring income, **we rate HTONSP 6.08% '21s with an Overweight recommendation as we see fair value around 5.75%**.

S&P: Not rated

Moody's: Not rated

Fitch: Not rated

Ticker: HTONSP

Background: HHL is a property company with assets and revenue predominantly in Singapore and UK. HHL focuses on property development, property investments and hospitality. HHL owns or holds stakes in 5 commercial properties and 8 hotel assets (with 3 more in the pipeline). The Toh family owns about 69% interest in HHL, which are represented by Heeton Investments Pte Ltd (27.63%), Hong Heng Co Pte Ltd (16.81%), Toh Giap Eng (11.96%), Toh Khai Cheng (6.79%) and Toh Gap Seng (5.78%).

Treasury Advisory

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Structured Products

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Interest Rate

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GT Institutional Sales

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Key credit considerations

- **Full year results lifted by disposal gains:** Revenue declined 15.2% y/y to SGD57.1mn, mainly due to lower recognition of revenue from property development, with Onze@Tanjong Pagar contributing less in 2017 (SGD29.8mn) than 2016 (SGD41.7mn). The second largest revenue contributor, from property investment, remained steady at SGD13.4mn (2016: SGD13.3mn). While the hospitality segment revenue contribution grew to SGD12.8mn (2016: SGD9.8mn), the segment profit results were disappointing with a loss of SGD0.9mn (2016 profit: SGD0.9mn). Despite weaker revenue, net profit surged to SGD71.6mn (2016: SGD12.2mn) with SGD28.0mn gain on disposal of The Lumos, fair value gain of SGD37.1mn in total from Tampines Mart (SGD11.0mn), The Woodgrove (SGD19.8mn) and Adam House in London (SGD6.6mn). Without the fair value and disposal gains, profit before tax would have fallen ~50% to SGD8.1mn, mainly due to an increase in personnel expense of 44.1% y/y to SGD11.2mn as HHL had increased headcount in the UK to ramp up hotel operations.

- **Double-edged sword from the recovery in the Singapore property market:** HHL has progressively moved more units at its fully-owned 56-units Onze@Tanjong Pagar which obtained TOP in Jan 2017, with SGD44.3mn in total sales (23 units) according to the URA caveats as of Dec 2017. At the associate and JV level, HHL has also completed and fully sold i) 20%-owned 480-units Westwood Residences, ii) 10%-owned 65-units Rezi3Two, iii) 12.25%-owned 142-units Floraville, Floravista and Floraview while 3 units at the 30%-owned 9-units 121 Collection on Whitley are sold. However, the optimism in the market appears to fuel aggressive land bids. HHL holds a 20%-stake in a Chip Eng Seng-led JV that won a SGD700.7mn land bid for a land parcel in Woodleigh and 5%-stake in an Oxley-led JV that acquired Serangoon Ville for SGD694mn.

- **Recurring income from investment properties:** Investment properties accounted for SGD13.4mn (out of SGD57.1mn) of 2017's revenue. This is likely mainly represented by the 100%-owned Tampines Mart and 100%-owned The Woodgrove (disposal completed in Feb 2018 for SGD56mn), which contributed SGD7.7mn and SGD2.5mn revenue respectively in 2016. The actual contribution from investment properties is higher, as the 50%-owned Sun Plaza's revenue is SGD9.8mn as of 9M2017 but is not included as part of HHL's revenue (part of income from associates). The fair value (as of 31 Dec 2017) of the wholly-owned investment properties amounts to SGD160.1mn (excluding The Woodgrove which is held for sale). Including non-wholly-owned investment properties (excluding The Woodgrove and Super Hotel Sapporo), we estimate total fair value at SGD337.8mn.

- **Expanding the hospitality portfolio:** With the opening of the 89-room Luma Concept Hotel in 2017, 7 hotels (884 rooms) are in operation (excluding the 20%-owned Super Hotel Sapporo in Japan). They contributed SGD12.8mn revenue in 2017, and this is likely to increase further with 3 more hotels in the pipeline, including the 70%-owned proposed 198-room hotel at 29 Ranwell Lane Fortitude Valley in Australia and the 55%-owned proposed 192-room hotel at New York Road, Leeds in UK. For the 50%-owned Dry Bar in UK, HHL is also proposing a redevelopment into a 110-120 room hotel. We estimate HHL's share of the fair value of the hotels at SGD128.6mn (or SGD99.8mn excl stakes below 50%).

- **Mediocre credit metrics though comfortable with profile due to asset backing:** Net gearing remained improved q/q to 0.65x (3Q2017: 0.72x), mainly due to the disposal of The Lumos which fetched proceeds of SGD15mn. 2017 cash inflow from operating activities of SGD42.8mn looks healthy, helped by sale of units at Onze@Tanjong Pagar. However, more cash may be required for the joint ventures at Woodleigh (with Chip Eng Seng) and Serangoon Ville (with Oxley). We remain comfortable with HHL as we estimate that its investment properties and hospitality portfolio (excl stakes 50% and below, and excluding The Woodgrove) is worth SGD267.6mn, which is comparable to the net debt of SGD268.7mn as of 4Q2017. This helps mitigate the smallish stakes in development projects which HHL has, which may be harder to monetize.

Discussions on expectation of increase in net gearing and potential use of proceeds

Although we expect 1Q2018 to record another SGD50.3mn cash inflow from the disposal of The Woodgrove (completed in Feb 2018), net gearing may reach ~0.8x if we assume SGD118mn bond proceeds that was raised in Jan 2018 to be fully consumed. While HHL has not specified precisely the use of proceeds, we think HHL could be undertaking one or several of the following:

1) **Likely expansion of hospitality portfolio.** This is likely and could come about from acquisitions of hospitality assets (investment and/or development), perhaps in Europe, as HHL has been ramping up its hospitality portfolio especially in the UK.
2) **Possible acquisition of further land sites in Singapore.** This is possible as HHL has been acquiring land sites (through JVs).
3) **Refinance.** HHL has SGD11.5mn of short-term bank loans and SGD82.4mn of bank term loans due within the next 12 months. However, as refinancing with another bank loan may be cheaper given the high coupon of 6.08%, the bond proceeds are more likely to be intended for 1) or 2).

View on the recent HTONSP 6.08% '21s

The recent SGD118mn 3.5-year HTONSP '21s was priced at 6.08%, tightening from an initial price guidance of 6.25% on the back of SGD150mn orderbook. **We see the fair value around 5.75%**, using the following for our consideration:

The closest comparable is the older HTONSP '20s, with HTONSP '21s offering 43bps pickup for 1.2Y extension. While the ~23bps yield spread pickup looks fair given the extension, we think that the HTONSP curve is trading too wide, in comparison to other peers.

Our fair value is derived by comparing to the recent OHLSP 5.7% '22s (YTM: 5.76%), as Oxley Holdings Ltd ("OHL") is similarly a developer and HHL and OHL are JV-partners for the development at Serangoon Ville. In our view, HTONSP '21s look very attractive sporting a higher yield to maturity, shorter duration and lower net gearing. We rated Oxley Holdings Ltd's ("OHL") with a lower Issuer Profile Rating of Negative (6), despite its significantly larger scale, given its very aggressive profile with numerous en-blocs and acquisitions (refer to Oxley Holdings Ltd: Credit Update on 14 Feb 2018).

Relative Value:

Bond	Maturity	Net gearing	Ask Yield	Spread
HTONSP 6.08% 2021	19/07/2021	0.65x	5.98%	396.3
HTONSP 6.1% 2020	08/05/2020	0.65x	5.55%	372.8
CHIPEN 4.75% 2021	14/06/2021	1.58x	3.93%	192.7
CHIPEN 4.9% 2022	19/05/2022	1.58x	4.23%	211.4
OHLSP 5.7% ‘2022	31/01/2022	1.86x	5.76%	367.1
GUOLSP 4.6% 2022	23/01/2023	0.84x	4.60%	241.3

Indicative prices as at 27 February 2018
Source: Bloomberg

In fact, **we think the HTONSP curve should be trading significantly tighter**. A closer comparable than OHLSP 5.7% ‘22s is CHIPEN 4.75% ‘2021. Trading at 5.98%, HTONSP 6.08% ‘21s provide 205bps yield pickup over CHIPEN 4.75% ‘21s (3.93%). As such, HTONSP 6.08% ‘21s (and HTONSP 6.1% ‘20s) look **extremely attractive in our view, and we see the potential for the HHL curve to rerate closer to CES (low ~4%)**. Chip Eng Seng Corp Ltd (“CES”), which we rated with an Issuer Profile of Negative (6), and HHL are JV partners for several large projects (e.g. High Park Residences, Woodleigh site). While CES is larger in scale (total assets: SGD2.7bn) compared to HHL (SGD823.7mn), HHL has a lower net gearing (0.65x) compared to CES (1.58x). HHL also has a larger proportion of recurring income from investment properties (e.g. Tampines Mart, Sun Plaza) and hotels.

Heeton Holdings Ltd

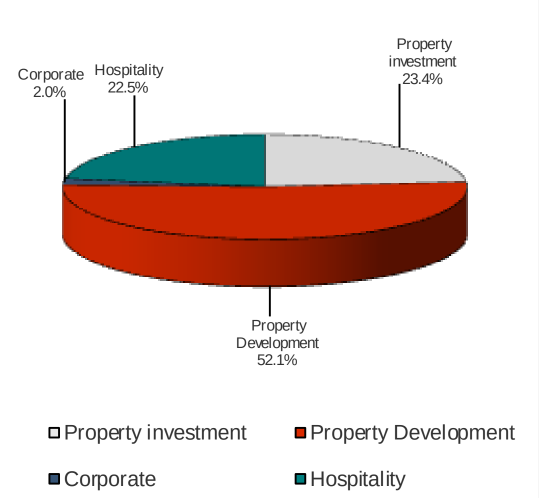
Table 1: Summary Financials

Year Ended 31st Dec	FY2015	FY2016	FY2017
Income Statement (SGD'mn)			
Revenue	34.3	67.4	57.1
EBITDA	9.4	16.6	3.9
EBIT	8.9	15.2	2.3
Gross interest expense	18.2	14.5	15.2
Profit Before Tax	4.7	17.1	73.2
Net profit	5.7	12.5	71.0
Balance Sheet (SGD'mn)			
Cash and bank deposits	22.3	27.8	22.9
Total assets	789.9	734.0	823.7
Gross debt	370.1	297.3	291.8
Net debt	347.8	269.5	269.0
Shareholders' equity	340.8	345.6	416.2
Total capitalization	710.9	642.9	708.0
Net capitalization	688.6	615.1	685.1
Cash Flow (SGD'mn)			
Funds from operations (FFO)	6.2	13.9	72.6
* CFO	-15.3	-6.8	42.7
Capex	37.8	28.0	14.2
Acquisitions	0.0	0.0	3.6
Disposals	0.2	4.2	15.0
Dividend	1.6	2.0	2.0
Free Cash Flow (FCF)	-53.1	-34.8	28.5
* FCF Adjusted	-54.5	-32.5	38.0
Key Ratios			
EBITDA margin (%)	27.5	24.6	6.8
Net margin (%)	16.5	18.5	124.3
Gross debt to EBITDA (x)	39.2	17.9	74.8
Net debt to EBITDA (x)	36.9	16.3	69.0
Gross Debt to Equity (x)	1.09	0.86	0.70
Net Debt to Equity (x)	1.02	0.78	0.65
Gross debt/total capitalisation (%)	52.1	46.2	41.2
Net debt/net capitalisation (%)	50.5	43.8	39.3
Cash/current borrowings (x)	0.1	0.1	0.2
EBITDA/Total Interest (x)	0.5	1.1	0.3

Source: Company, OCBC estimates

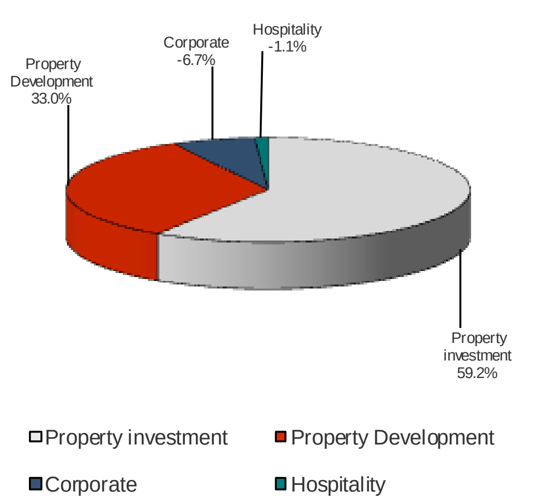
**FCF Adjusted = FCF - Acquisitions - Dividends + Disposals | *CFO after deducting interest expense*

Figure 1: Revenue breakdown by Segment - FY2017



Source: Company

Figure 2: PBT breakdown by Segment - FY2017



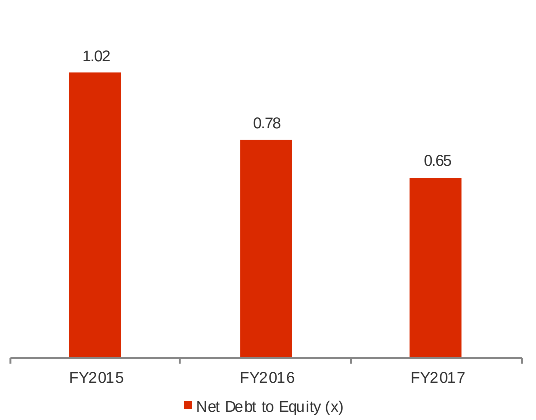
Source: Company

Figure 3: Debt Maturity Profile

Amounts in (SGD'mn)	As at 31/12/2017	% of debt
Amount repayable in one year or less, or on demand		
Secured	90.0	30.8%
Unsecured	4.0	1.4%
	94.0	**32.2%**
Amount repayable after a year		
Secured	122.8	42.1%
Unsecured	75.0	25.7%
	197.8	**67.8%**
Total	**291.8**	**100.0%**

Source: Company, OCBC estimates

Figure 4: Net Debt to Equity (x)



Source: Company

Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Explanation of Bond Recommendation

Overweight ("OW") – The performance of the issuer's specific bond is expected to outperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Neutral ("N") – The performance of the issuer's specific bond is expected to perform in line with the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.

Underweight ("UW") – The performance of the issuer's specific bond is expected to underperform the issuer's other bonds, or the bonds of other issuers either operating in the same sector or in a different sector but with similar tenor over the next six months.