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# Heeton and the "Naked Stay" : How One Company Is Trying to Revolutionize Global Travel

**Can a home-grown property developer disrupt the hospitality industry with its new hotel concept? We reveal the secret of Heeton's "Naked Stay", and tell you why bond investors should pay attention to this company.**

by Linus Tham

17 Jun 2019 • 16 min(s) read



## Introduction

Situated along Glenthorne Road in the cultured suburban district of Hammersmith, London, Luma London is a hotel unlike any other. Conceptualized by Heeton Holdings Limited, Luma London promises guests a 'naked stay': accommodation free from unwritten rules and accepted conventions.

Guests stepping into Luma London for the first time might be taken aback by the absence of amenities considered de rigueur in other hotel establishments. There is no on-site restaurant at Luma or any celebrity chef that typically comes with it. Guests will not find a spa on the premises either, or the usual expansive ballrooms that come with any five-star establishment.

Instead, Luma London promises guests its trademark 'perceptive' and 'personalized' service, an experience designed for and around the guest. Where most hotels constrain guests to checking in after 3pm, Luma London provides the assurance that guests would be welcomed 'just as warmly at 3am'.

Breakfast at Luma London is also freshly made and ready for pick up at any time of the day, unlike most hotel breakfast buffets that close by 9 or 10 in the morning. The concierge service is not limited to concert tickets and restaurant bookings either; Luma London is the one-stop shop for everything that the guest might need, from clutch bags to cufflinks, lemon tea to lavender oil.

The absence of full-service hotel facilities notwithstanding, Luma London is located right in the heart of Hammersmith, arguably one of London's most thriving suburban districts. The nearby Knightsbridge offers a world-class shopping experience; the world-famous Harrod's departmental store replete with all manner of luxury goods, exquisite delicacies, and a restaurant for every taste. Cultural institutions are also not far away, with the Natural History Museum in South Kensington just a stone's throw away.



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by Dexter Tan

Luma London, Heeton's first concept hotel in its stable of hospitality properties, was opened in April 2017. A hotel with just 89 rooms with each room spanning less than 200 square feet, Luma London was developed by a Heeton-led consortium, in which Heeton Holdings holds a 60% stake. The other partners in the consortium are KSH, Lian Beng, and Ryobi Kiso.

In opting to build a boutique hotel without any of the usual facilities associated with such establishments, Heeton created a product that would ultimately prove successful with modern millennial travelers, who typically eschew hotel facilities in favor of time spent outdoors.

As Mr Eric Teng, chief executive of Heeton Holdings, noted in a [wide-ranging interview](#) with the local newspaper 'The Straits Times', 'We found that guests either don't use the facilities much or they are out of the hotel most of the time. We recognize a gap to fill, where a lot of people want good-quality rooms but limited services usage.'

In fact, Heeton does not exclude the possibility of rolling out the Luma Concept to other markets in the future, given the firm's success both with the Luma brand and in the hospitality sector in general.

When Luma was first introduced to London, hospitality accounted for just over 10% of the property firm's aggregate revenue. Today, Heeton derives almost a third of its revenue from the hospitality sector. In 2018, hospitality revenue accounted for 31.95% of total group revenue.

Heeton's rapid growth in hospitality stems in part from the company's aggressive efforts in developing new ideas such as Luma. Acquisitions have also been a large part of the group's strategy.

In April 2018, a Heeton-led consortium made up of Heeton, KSH Holdings, and Ho Lee Group acquired the Crowne Plaza London Kensington hotel for GBP 84.3 million. At the point of acquisition, the property had an annual turnover of GBP 11.8 million.

In October, the group made its foray into Scotland by acquiring the Stewart Apartments in Edinburgh, a development with 31 apartment units. The group also acquired Hotel Indigo in Glasgow, a five-storey hotel with 94 rooms operating under a franchise agreement with Intercontinental Hotels Group. Later in the same year, Heeton announced that it had acquired a development site in the Kingdom of Bhutan, with a view to developing it into a luxury hotel complex.

Much can be learnt from how Heeton managed to reshape its business over the years, from its humble beginnings as a local property developer when it was first founded in 1976, to the rapidly growing enterprise that is presently making inroads in the international hospitality scene. But Heeton is more than just about hotel operations. It is in fact a multi-faceted property developer as well, operating in most of the major property segments. We invite you, our esteemed readers, to join us as we embark on a detailed tour of Heeton's business.

### ***How Heeton Makes Its Money***

We begin with a brief overview of what Heeton does, for the benefit of readers who might not have heard of or are unfamiliar with Heeton.

At its core, Heeton is a property developer, investor, and operator. As a property developer, the company purchases land and adds value to it by building residential or commercial buildings. Because Heeton is not involved in the construction business, building construction is usually reserved to third-party contractors.

Heeton is also a property investor, in the sense that it acquires various investment properties for the express purpose of collecting rental income.

Acting as a property operator is slightly more complex. As a property operator, Heeton might acquire the underlying property and operate it with the benefit of a franchise agreement.

This can be best understood in the context of the hospitality industry, a sector in which Heeton employs this model frequently. In 2015, Heeton acquired the Ibis Budget Bradford from the Accor Group ('Accor'), an 86-room hotel in the city of Bradford. Located just 12 miles from the city airport, the hotel benefits from easy access to the nearby cities of Leeds and Manchester, the capital of



northern England. After the acquisition, Heeton signed a new franchise agreement with Accor. Under this agreement, Heeton would continue to operate the hotel under the 'Ibis' brand name (a brand owned by Accor), with franchise and licensing fees paid to Accor accordingly.

In 2018, Heeton derived approximately 44.0% of its revenue from property development. The bulk of this came from revenue generated from developing various residential projects in Singapore. 34.0% of aggregate revenue came from hotel operations and management fees, including those generated from the Ibis Budget Bradford hotel described in the preceding paragraph. Slightly more than one-fifth of group revenue could be attributed to property investment activities (i.e. rental income).

A brief mention should be made about the nature of these revenue streams. Property development, a process which involves the purchase and sale of land and developed buildings, is inherently cyclical. In other words, revenue from property development depends largely on which phase of the economic cycle the country is in.

Among the two major factors that impact this segment is the availability and cost of land, and the ability of the developer to sell completed units to the public. Both factors depend largely on macroeconomic conditions, with the former shaped by government policy in most cases. Hence, property development revenue should be regarded as being somewhat cyclical or variable in nature.

In contrast, revenue from property management and investment tends to be more stable due to its recurring nature. Remembering that about 56% of Heeton's revenue comes from these sources (and only 44% coming from cyclical property development), we think that this is a positive attribute of Heeton's revenue profile.

Heeton derives all of its revenue from its core markets of Singapore and the United Kingdom. Even though Heeton has established itself in Singapore, the group has made significant efforts in internationalizing its operations over the years. In 2018, revenue from Singapore and the United Kingdom accounted for 59.7% and 40.4% of group revenue, respectively. As recently as 2017, Singapore accounted for over 70% of total revenue.

Much of Heeton's growth over the years came from the company's property management division. In 2018, revenue from hotel operations and other property management was S\$18.7 million, representing a growth rate in excess of 34% year-on-year ('YoY'). Such a rate of growth is impressive and certainly bears witness to the management's single-minded determination to growing the company's recurring revenue stream.

So far, our analysis of Heeton's revenue profile has focused on product and geographical segmentation. For the purpose of obtaining a more complete picture, let us look at Heeton's very recent financial performance.

### ***Heeton's 1Q19 Earnings Performance***

For the three months ended 31 March 2019, revenue for the quarter was S\$11.1 million (1Q18: S\$11.9 million). The YoY revenue decline of 6.1% notwithstanding, this should be analyzed in the context of the wider property sector and how Heeton's peers performed. CapitaLand Limited, a company with significant exposure to Singapore as well, saw its revenue decline some 23.8% YoY over the same period. Given the context, it would probably not be too far-fetched to say that Heeton had outperformed the market by a large degree.

One aspect of Heeton's business that might be of interest is the company's proclivity for joint ventures, to the point that the company actually derives a significant part of its earnings from the various joint ventures it has with third parties. For the first quarter of 2019, the share of results of associated companies and joint ventures formed some 13.0% of Heeton's EBIT. In the first quarter of the previous year, earnings from these partnerships contributed a full 35.9% of group EBIT, or some S\$3.5 million (out of total EBIT of S\$9.6 million).

Some snapshots of Heeton's modus operandi. In April this year, a consortium led by Heeton Holdings (with a 60% stake), teamed up with Singapore-listed contractor KSH Holdings and construction company Ho Lee Group (each holding 20% in the venture), to acquire Crowne Plaza London Kensington hotel for GBP 84.3 million (S\$148.9 million). The hotel, located in the London Borough of Kensington and Chelsea and tucked behind a historic Georgian facade, posted a turnover



of GBP 11.8 million in 2018.

The informed reader would have noted that at the point of purchase, Heeton's market capitalization was only S\$154.4 million. The transaction, valued at almost S\$150 million, was nearly the same size as Heeton's market capitalization. This observation points to the underlying rationale for Heeton's joint ventures.

Far from being risk averse, it is clear that Heeton has no difficulty engaging in risky, big-ticket deals. But if it had transacted in these deals alone, it would have had to bear significant idiosyncratic risk. It is also not certain whether Heeton could have accessed the desired levels of financing for these deals.

Moreover, Heeton typically takes a controlling stake in many of these joint ventures, giving it overall operational control of the project, while limiting the financial exposure associated with the project. This appears to be a very enlightened approach to property development, which is particularly suited to Heeton's reality as a medium-sized company that does not benefit from the resources that large real estate behemoths possess.

In the next section, we will undertake a comprehensive study of Heeton's balance sheet : its assets and liabilities. As bond investors, it is important to not just understand the company's sources of revenue, but also to understand whether the company possesses sufficient assets to covers its debt, including its outstanding bond issues.

### ***Heeton's Balance Sheet: Assets and Liabilities***

The first thing to note is that Heeton is an asset-rich company, with ample cash resources and property holdings. At the end of March 2019, the company had S\$89.3 million in cash and cash equivalents (December 2018: S\$75.0 million), an increase of 19% quarter-on-quarter ('QoQ'). Heeton also has a significant amount of property and land assets. As of 31 March 2019, the company had S\$396.4 million in land and property assets (excluding development properties). Including development properties, this figure goes up to S\$427.1 million.

Given its ample cash, it should come as no surprise that Heeton scores well in liquidity. Its current ratio, measured as the ratio of current assets over current liabilities, was 1.42 as at end March 2019 (December 2018: 1.32).

The evolution of Heeton's cash ratio also paints a similar picture of enhanced access to liquidity. At the end of March 2019, its cash ratio (cash and cash equivalents divided by current liabilities) was 0.71 (December 2018: 0.60)

Relative to its assets, Heeton carries little debt for a property development company. Its gearing ratio, defined as total debt divided by total assets, was stable at 0.39x (31 December 2018: 0.38x). As of 31 March 2019, the company had S\$105.1 million in debt maturing within a year, and S\$235.6 million in longer term debt. This works out to just 30.8% of its total debt maturing within a year. When we consider the fact that Heeton had almost S\$90 million in cash and cash equivalents, and that the S\$105.1 million of short-term borrowings comprise fully of secured bank loans (which we think could be refinanced with relative ease), we can conclude that the risk of a near-term liquidity shock is manageable.

We also wish to take this opportunity to draw the reader's attention to an important observation. Not only is Heeton an asset-rich company, its property assets are also relatively unencumbered. The company has S\$396.4 million in fixed assets and investment properties (excluding development properties), compared to S\$147.7 million of secured borrowings, which translates to an implied loan-to-value ratio of 37.2%.

Heeton's two outstanding bonds consist of a S\$75 million issue maturing in May 2020 and another S\$118 million bond maturing in July 2021. Assuming a loan-to-value of 50%, we think the company should be able to raise additional S\$51m of secured borrowings if needed. This, combined with the cash resources at Heeton's disposal, and the company's pipeline of development projects as well as its recurring revenues, should provide Heeton with the means to meet its financial obligations.

Furthermore, we understand that the directors of Heeton currently own S\$4.25 million of the S\$75 million bonds maturing in 2020 and S\$5.75 million of the S\$118 million bonds maturing in 2021. In

aggregate, this represents 5% of the total outstanding bonds that is owned by company insiders. The necessary implication is that any eventual default would involve the directors suffering some degree of financial harm, at a personal level. For bond investors, this should provide a degree of assurance that the directors have their interests aligned with those of the bondholders.

## Comparing the Heeton Bonds

Figure 1: Heeton Bonds

Bond Ticker	Coupon Rate (%)	Time to Maturity	Ask Price	Ask YTM (%)	Z-spread (Ask; bps)	Issue Size (\$m)
HTONSP 6.100% 08May2020 Corp (SGD)	6.10	0.9	99.52	6.65	489	75
HTONSP 6.080% 19July2021 Corp (SGD)	6.08	2.1	97.55	7.36	570	118

Source: Bloomberg, iFAST compilation; pricing data as of 14 June 2019

The reader might recall that earlier in the article, we alluded to Heeton having two outstanding bond issues. One of them matures in May 2020 (time to maturity: 1 year) and yields 6.65%, while the other matures in July 2021 and yields 7.36%.

Given a choice between a Heeton bond maturing in a year's time (with a yield of slightly more than 6%) and another Heeton bond maturing in 2.2 years' time (with a yield of about 7%), which would be the better option?

One factor in favour of the [HTONSP 6.08% 19July2021 Corp \(SGD\)](#) is its larger issue size of S\$118 million, compared to the S\$75 million issue size of the [HTONSP 6.100% 08May2020 Corp \(SGD\)](#). This means that in the case of [HTONSP 6.08% 19July2021 Corp \(SGD\)](#), liquidity in the secondary market would probably be better, an important consideration if the investor wishes to sell his holdings before maturity.

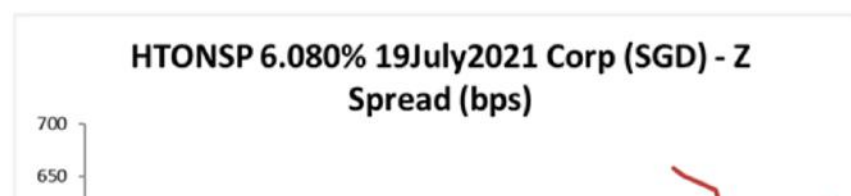
As a practical matter, an investor buying into a bond that matures within a year might also have to contend with increased trading costs and rollover risks (the need to reinvest the money within a year).

Astute bond investors also know that not only is it important to choose the right bond issue, it is equally important to effect the purchase at the best possible price, and at the right time. In this regard, we present a chart which shows the evolution of the HTONSP 6.08% '21s' Z-spread over a one-month period.

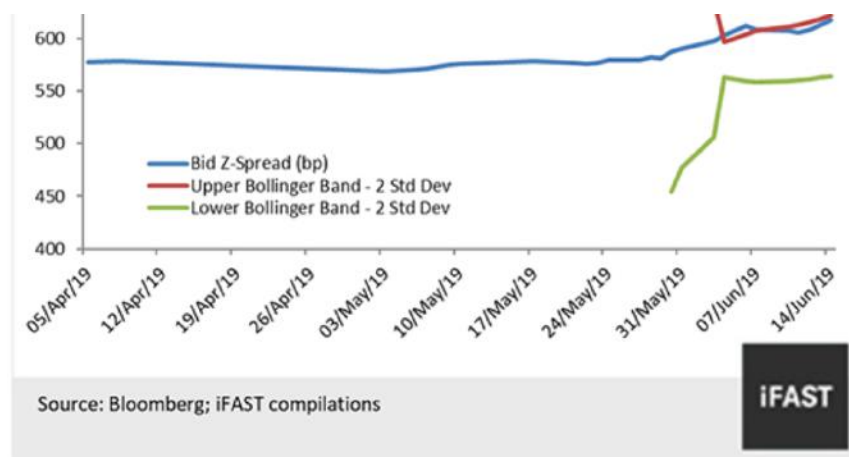
The reader would quickly notice from the graph that not only is the bond's Z-spread trading at a high, it is also trading at close to the 2 standard deviations upper bracket. To digress briefly, the 2 standard deviations upper and lower brackets are plotted 2 standard deviations above and below, respectively, the simple moving average of the bond's Z-spreads.

The fact that the Z-spread is currently trading close to the 2 standard deviations upper limit provides us with yet another indication on the bond's current attractive valuation.

Figure 2: HTONSP 6.08% 19July2021 Corp (SGD) : Z-Spread







## Relative Valuation

The skeptical reader might argue that simply because one Heeton bond is more attractive relative to the other, it does not necessarily mean that the Heeton bonds are attractive purchases in the first place.

We agree.

To address this question, we look at how bonds issued by other companies are trading. Naturally, it would only be appropriate to compare bonds of similar tenures i.e. a bond issued by Heeton maturing in 2 years should be compared with a bond issued by Chip Eng Seng that also matures in 2 years' time.

Figure 3: Peer Comparison

Bond	Coupon Rate (%)	Time to Maturity	Ask Price	Ask YTM (%)	Reference Security	Reference Security Yield (%)
Chip Eng Seng 4.75% 14June2021 Corp (SGD)	4.75	2.0	97.96	5.85	HTONSP 6.080% 19July2021 Corp (SGD)	7.36
Tuan Sing Holdings 6.00% 05June2020	6.00	1.0	99.61	6.42	HTONSP 6.100% 08May2020 Corp (SGD)	6.65

Source: Bloomberg, iFAST compilation; pricing data as of 14 June 2019

In the first row, the reader will readily observe that the [HTONSP 6.080% 19July2021 Corp \(SGD\)](#) bond bears a higher yield of 7.36%, significantly more attractive than the comparable security issued by Chip Eng Seng, another real estate developer in Singapore. Besides, Chip Eng Seng is more highly geared than Heeton, with a debt-to-asset ratio in excess of 50%.

In the second row, we compare Heeton's 2020 bond to Tuan Sing Holdings' notes maturing in June 2020. Immediately noticeable is the fact that their yields are comparable. However, we might also like to take into account that Heeton has a much better liquidity situation compared to Tuan Sing. Reflective of this is Tuan Sing's current ratio of just 0.62, which pales in comparison to Heeton's current ratio of 1.42.

## Conclusion

One of Heeton's greatest assets is its far-sighted management team, which has relentlessly focused on reducing the company's reliance on the cyclical property development business by developing new sources of revenue in the hospitality scene. Luma London is, of course, the most prominent example of these efforts.

Taken as a whole, we believe that Heeton is a company that bond investors should consider including in their portfolio. Our confidence stems from Heeton's strong recurring income stream

(one that is growing strongly) and overall healthy balance sheet. Furthermore, our analysis demonstrates the attractive valuation of its bonds, particularly in the case of Heeton's [HTONSP 6.080% 19July2021 Corp \(SGD\)](#).

#### Declaration:

*For specific disclosure, at the time of publication of this report, IFPL (via its connected and associated entities) has a principal position in HTONSP 6.100% 08May2020 Corp (SGD). The analyst who produces this report own none of the above mentioned securities.*

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