Research Update:

Hypera S.A. Downgraded To 'BB' On Higher-Than-Expected Leverage; Outlook Stable

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Rating Action Overview

- Brazil-based pharmaceutical company Hypera S.A. reported net revenue of Brazilian real (R$) 7.4 billion, adjusted EBITDA of R$2.1 billion, and adjusted debt to EBITDA of 4.0x in the 12 months ended December 2024.
- We expect adjusted debt to EBITDA to remain above 3.0x over the next 12 months because of the decrease in profitability stemming from changes in the company's working capital policy.
- Although we expect operating cash flow to partially mitigate the higher leverage, we believe macroeconomic challenges will create execution risks for the company's strategy for the next two years.
- Consequently, we lowered our global scale long-term issuer credit rating on Hypera to ‘BB’ from ‘BB+’ and lowered our Brazil national scale issuer credit and issue ratings to ‘brAA+’ from ‘brAAA’.
- The stable outlook reflects our expectation that the company will be able to recover its revenue, EBITDA, and margins while improving the distribution and delivery of its products over the coming months and continuing to generate strong cash flow.

Rating Action Rationale

We expect the effects of changes in the working capital policy will become evident in 2025. In October 2024, Hypera informed the market that after internal discussions, it had decided to start optimizing working capital by reducing the payment term policy granted to customers. The aim of the process would be to increase operating cash generation, according to the statement issued by the company, by R$2.5 billion by 2028 and R$7.5 billion over the next 10 years. Hypera's management believes this strategy can increase financial flexibility to capture growth opportunities, as well as improve operational efficiency.

Meanwhile, the results for the fourth quarter of 2024 showed a quarterly drop of 18.2% in net revenue and 74.6% in EBITDA from continuing operations. Year on year, net revenue and EBITDA from continuing operations fell by 6% and 23.8%, respectively. These drops resulted in much higher leverage than we expected, with the company reporting adjusted debt to EBITDA of 4.0x, compared with our previous forecast of 2.7x by the end of 2024. Given the hit to revenue and profitability, we expect adjusted debt to EBITDA to remain around 3.4x in 2025, up from our previous forecast of 2.0x.

Hypera has stated that with the conclusion of working capital optimization in 2025, its product stocks with customers will reach levels commensurate with the overall pharmaceutical industry in Brazil, without compromising the sales volume forecast for the coming years, the remuneration of its shareholders, or planned investments. We therefore project revenue of R$8 billion-R$10 billion and EBITDA of R$3 billion over the next two years, with margins of 26% in 2025 and 34% in 2026. But macroeconomic challenges, with rising interest rates, high inflation, and weakening GDP growth, will create execution risks for the company's strategy.

Strong cash flow partially mitigates Hypera's exposure to short-term obligations and higher leverage. The company has generated consistently satisfactory cash flow and maintained prudent liability management, especially of its short-term obligations. Despite the contraction in results and the consequent increase in leverage, we expect Hypera will maintain its ability to honor its obligations and related interest expenses, gradually increasing adjusted operating cash flow in relation to debt to 28%-30% in 2025 and 2026.

We expect operating cash flow to cover interest expenses and our forecast annual capital expenditure (capex) and intangible acquisitions of about R$850 million, with the remainder distributed to shareholders through interest on own capital. As a result, we forecast discretionary cash flow (DCF) generation from 2025 on.

We believe Hypera's robust brand portfolio can help balance its higher leverage. We expect leverage to gradually decrease over the next few years as the company focuses on completing the working capital optimization and improving the research and development pipeline. In our base case, we expect adjusted net debt to EBITDA will be around 3.4x at the end of 2025, then fall to 2.1x in 2026.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that Hypera will recover its credit metrics, albeit slowly, alongside more conservative liability management, which will keep its liquidity comfortable in the coming years. We expect the reorganization of the company's working capital to strengthen its cash generation and reduce its adjusted leverage, with adjusted debt to EBITDA of 3.4x at the end of 2025 and closer to 2.0x from 2026 on.

Downside scenario

We could downgrade Hypera in the next 12 months if the company's credit metrics weaken and it fails to deliver the expected recovery in EBITDA and leverage. In this scenario, adjusted debt to EBITDA would remain above 3.5x, with consistently negative DCF and tightened liquidity.

Upside scenario

We could upgrade Hypera in the next 12 months following a faster-than-expected drop in leverage and accelerated EBITDA growth, with the company maintaining its conservative approach to debt. In this scenario, adjusted net debt to EBITDA would be consistently below 3.0x and DCF to debt above 10%.

Company Description

Headquartered in São Paulo, Hypera S.A. is a publicly traded company, listed on the Novo Mercado and with shares on the São Paulo stock exchange (B3 S.A.). As one of the main pharmaceutical companies in the Brazilian market, Hypera is a leader in several segments and sells products that are highly popular in Brazil.

Hypera's main distribution center is in Anápolis, a city in the Brazilian state of Goiás. Production takes place mainly at the Brainfarma and Cosmed subsidiaries, also located in Goiás, with a new unit in Itapecerica da Serra, in the state of São Paulo.

Research and product development are centralized in Brainfarma's innovation center in Barueri, which has technologies for various pharmaceutical forms in its six laboratories. The company also has a vast sales and distribution structure that covers the whole of Brazil, serving both retailers directly and through distributors.

Our Base-Case Scenario

Assumptions

- Brazil’s GDP growth at 1.9% in 2025, 2.0% in 2026, and 2.1% in 2027.
- Brazilian inflation (consumer price index) at 5.2% in 2025, 4.7% in 2026, and 3.8% in 2027.
- Base interest rates of 14.6% in 2025, 13.1% in 2026, and 10.4% in 2027.
- Annual revenue growth of 9.8% in 2025, around 20.1% in 2026, and 11% in 2027, following expected revenue recovery after the working capital optimization.
- Stable margins of 64%-65% in the next three years.
- Annual capex and intangible acquisitions of around R$850 million in the next three years.
- We assume the company will issue new debt to refinance short-term maturities.

Key metrics

Hypera S.A.--Forecast summary

Period ending	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026	Dec-31-2027	Dec-31-2028
(Mil. BRL)	2021a	2022a	2023a	2024a	2025e	2026f	2027f	2028f
Revenue	5,937	7,546	7,915	7,442	8,172	9,814	10,894	12,070
Gross profit	3,935	4,931	5,234	4,662	4,966	6,368	7,085	7,843
EBITDA (reported)	2,100	2,652	2,756	2,101	2,185	3,393	3,877	4,381
Plus: Operating lease adjustment (OLA) rent	--	--	--	--	--	--	--	--

Hypera S.A.--Forecast summary

Plus/(less): Other	(37)	23	(9)	(76)	(24)	(24)	(24)	(24)
EBITDA	2,063	2,674	2,747	2,025	2,161	3,369	3,853	4,357
Less: Cash interest paid	(308)	(867)	(1,306)	(1,195)	(1,158)	(1,442)	(1,330)	(1,122)
Less: Cash taxes paid	(7)	(6)	(4)	(8)	299	(81)	(189)	(222)
Plus/(less): Other	--	--	--	--	--	--	--	--
Funds from operations (FFO)	1,748	1,801	1,436	823	1,302	1,846	2,334	3,013
EBIT	2,011	2,695	2,669	1,935	2,176	3,423	4,019	4,767
Interest expense	383	986	1,129	971	1,157	1,439	1,328	1,120
Cash flow from operations (CFO)	1,153	1,312	1,236	1,420	2,330	2,049	2,538	3,665
Capital expenditure (capex)	839	1,509	813	772	550	580	370	385
Free operating cash flow (FOCF)	314	(198)	423	648	1,780	1,469	2,168	3,280
Dividends	746	806	760	787	649	644	644	644
Share repurchases (reported)	129	87	88	56	--	--	--	--
Discretionary cash flow (DCF)	(560)	(1,091)	(425)	(196)	1,131	825	1,524	2,636
Debt (reported)	7,361	9,608	9,938	9,380	8,686	8,886	8,986	9,486
Plus: Lease liabilities debt	89	121	218	208	228	274	304	337
Plus: Pension and other postretirement debt	--	--	--	--	--	--	--	--
Less: Accessible cash and liquid Investments	(2,287)	(2,862)	(2,581)	(1,739)	(1,777)	(2,347)	(3,503)	(6,109)
Plus/(less): Other	427	745	449	317	317	317	317	317
Debt	5,589	7,611	8,024	8,165	7,454	7,130	6,104	4,031
Equity	9,833	10,655	11,518	12,102	12,771	14,030	15,888	18,669
FOCF (adjusted for lease capex)	245	(306)	220	461	1,700	1,368	2,086	3,199
Interest expense (reported)	383	986	1,129	971	1,157	1,439	1,328	1,120
Capex (reported)	839	1,509	813	772	550	580	370	385
Cash and short-term investments (reported)	2,287	2,862	2,581	1,739	1,777	2,347	3,503	6,109
Adjusted ratios								
Debt/EBITDA (x)	2.7	2.8	2.9	4.0	3.4	2.1	1.6	0.9
FFO/debt (%)	31.3	23.7	17.9	10.1	17.5	25.9	38.2	74.7
FFO cash interest coverage (x)	6.7	3.1	2.1	1.7	2.1	2.3	2.8	3.7
EBITDA interest coverage (x)	5.4	2.7	2.4	2.1	1.9	2.3	2.9	3.9
CFO/debt (%)	20.6	17.2	15.4	17.4	31.3	28.7	41.6	90.9
FOCF/debt (%)	5.6	(2.6)	5.3	7.9	23.9	20.6	35.5	81.4
DCF/debt (%)	(10.0)	(14.3)	(5.3)	(2.4)	15.2	11.6	25.0	65.4
Lease capex-adjusted FOCF/debt (%)	4.4	(4.0)	2.7	5.6	22.8	19.2	34.2	79.4
Annual revenue growth (%)	45.2	27.1	4.9	(6.0)	9.8	20.1	11.0	10.8
Gross margin (%)	66.3	65.3	66.1	62.6	60.8	64.9	65.0	65.0
EBITDA margin (%)	34.7	35.4	34.7	27.2	26.4	34.3	35.4	36.1
Return on capital (%)	15.5	16.0	14.1	9.7	10.7	16.5	18.6	21.3
Return on total assets (%)	10.8	12.4	11.1	7.9	8.9	13.5	14.9	16.0

Hypera S.A.--Forecast summary								
EBITDA/cash interest (x)	6.7	3.1	2.1	1.7	1.9	2.3	2.9	3.9
EBIT interest coverage (x)	5.2	2.7	2.4	2.0	1.9	2.4	3.0	4.3
Debt/debt and equity (%)	36.2	41.7	41.1	40.3	36.9	33.7	27.8	17.8
Debt fixed-charge coverage (x)	5.4	2.7	2.4	2.1	0.8	1.5	1.7	1.7
Debt/debt and undepreciated equity (%)	36.2	41.7	41.1	40.3	36.9	33.7	27.8	17.8

All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast. R$--Brazilian real.

Liquidity

We view Hypera's liquidity as adequate. We expect cash sources to exceed uses by more than 20% over the next 12 months, given the company's cash position and expected funds from operations (FFO) are more than sufficient to cover short-term maturities and discretionary cash outflows. We expect net cash inflows to remain positive even if EBITDA falls by 15% compared with our base case, and Hypera should continue to meet the limits of its covenants with a cash cushion of more than 30%.

Principal liquidity sources

- Cash position of R$1.7 billion as of Dec. 31, 2024.
- Cash FFO generation of about R$2.4 billion in the 12 months from Dec. 31, 2024.
- Debenture issued January 2025 of R$530 million.

Principal liquidity uses

- Short-term debt of R$1.3 billion as of Dec. 31, 2024.
- Intangible acquisitions of R$340 million in the next 12 months.
- Capex of about R$550 million in the next 12 months.
- Dividend distribution of about R$649 million for the next 12 months.

Covenants

The covenants attached to the company's debt require net debt to EBITDA of less than 3.75x. We expect Hypera to maintain a comfortable margin under these covenants. As of Dec. 31, 2024, restrictive clauses had been met, and the next measurement of the reported ratio will take place June 30, 2025.

Issue Ratings--Recovery Analysis

Key analytical factors

We analyze Hypera's recovery prospects using a simulated default scenario with an EBITDA multiple valuation approach. Our simulated default scenario assumes a hypothetical payment default in 2030. The default would result from a severe economic slowdown, changing consumer behavior amid reduced discretionary income, and heightened competition in the pharmaceutical industry, leading to a decline in cash flow.

We use a going-concern assumption with a 6.5x multiple for our projected emergence EBITDA, in line with industry peers. We do so because we believe the company would likely be restructured--rather than liquidated--in an event of default, given its strong position in Brazil's pharmaceutical industry, with well-known brands and solid operations that should generate consistent cash flow. We also believe the company would be able to refinance its debt.

In our simulated default scenario, we estimate EBITDA would plunge about 70% from the 2025 forecast, triggering a hypothetical payment default. At that level, we estimate the company's cash flow would be insufficient to cover interest expenses and maintenance capex.

S&P Global Ratings limits the recovery rating to ‘3’ and the credit rating for unsecured debt issues in Group B jurisdictions, including Brazil. This limitation reflects the lower support for Brazilian creditors due to the lower enforceability and predictability of insolvency laws, as well as rule-of-law risk considerations, which, in our opinion, limit recoveries for creditors in this group.

Simulated default assumptions

- Year of the hypothetical default: 2030
- Country of insolvency: Brazil (Jurisdiction B), leading to a jurisdictional ceiling of '3' for unsecured debt
- Emergency EBITDA: R$1.1 billion
- Applicated EV multiple: 6.5x
- Estimated gross EV in emergency: R$7.2 billion
- Estimated net EV, after administrative expenses of 5%: R$6.8 billion

Simplified waterfall

- Senior secured debt: R$482 million (Finep and BNDES)
- Senior unsecured debt: R$8.8 billion (existing bank loans and debentures)
- --Recovery expectations for the unsecured debt: 50%-70% (rounded estimate: 65%; jurisdiction cap for senior unsecured debt)

Note: All debt amounts include six months of prepetition interest.

Rating Component Scores

Rating Component Scores	
Foreign currency issuer credit rating	BB/Stable/--
Local currency issuer credit rating	BB/Stable/--
Business risk	4 - Fair
Country risk	4 - Moderately high risk
Industry risk	2 - Low risk
Competitive position	4 - Fair
Financial risk	4 - Significant
Cash flow/leverage	4 - Significant
Anchor	bb
Diversification/portfolio effect	3 - Neutral/undiversified
Capital structure	Neutral
Financial policy	Neutral
Liquidity	Adequate
Management and governance	Neutral
Comparable rating analysis	Neutral
Stand-alone credit profile	bb

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings list		
Downgraded		
	To	**From**
Hypera S.A.		
Issuer Credit Rating	BB/Stable/--	BB+/Stable/--
Brazil National Scale	brAA+/Stable/--	brAAA/Stable/--
Downgraded; Recovery Ratings Unchanged		
	To	**From**
Hypera S.A.		
Senior Unsecured	brAA+	brAAA
Recovery Rating	3(65%)	3(65%)