



ISSUER RATING

Long-term Rating

Outlook: Stable

First rating date: 06/09/2019

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Rating Action and Rationale

- EthiFinance Ratings upgrades Grupo Pestana, SGPS, S.A's rating from "BBB-" to "BBB", changing its outlook from Positive to Stable.
- The change in the rating is based on the positive evolution of all financial metrics in 2022 and as of September 2023 evidenced by a low indebtedness level, a high level of financial autonomy and a good interest coverage ratio.
- The rating is supported by the group's solid financial profile, including the low level of indebtedness (NFD/EBITDA <2.0x and FFO/NFD ~50% on average) together with a strong loan-to-value ratio (below 30%).
- On the other hand, the rating is constrained by the still modest size of the company, which affects its overall competitive positioning, together with its high exposure to the Portuguese market and the leisure segment. In addition, its ownership structure limits the amount of financial support potentially available in stress scenarios.
- In line with our methodology, the hotel sector presents a medium to low ESG risk (sector heatmap score between 2.0 and 2.9) given its limited impact on the environment. This assessment has a neutral impact on the sector assessment. The company's ESG policy is considered to be adequate (company ESG score between 1 and 4), also resulting in a neutral impact on the overall rating.

Issuer Description

Grupo Pestana, SGPS S.A is a Portuguese company, founded in 1972, which focuses its activity on the tourist sector. The company is the Portuguese subsidiary of Pestana International Holding (PIH), the largest group in the hospitality business in Portugal. The company manages 82 facilities in Portugal under Pestana Hotels, Pestana Collection, Pestana CR7, Pousadas de Portugal and Pestana Residences brands. The group's offer is complemented by real estate activities, golf courses and the Casino da Madeira. The company's turnover in 2022 amounted to €375.4m (+43.2% YoY), with EBITDA of €128.9m and an EBITDA margin of 34.3%. NFD/EBITDA stood at 2.2x. In 9M 2023, the company's turnover amounted to €363.8m, with EBITDA of €131.7m and an EBITDA margin of 36.2%. NFD/EBITDA LTM was down to 1.7x.

In assigning the rating, the financial projections provided by Grupo Pestana and PIH for the period 2023-2024 have been taken into account. The company considers this information to be internal and confidential and therefore it has not been reflected in this report.

Fundamentals

Business Profile

Industry Risk Assessment

- Sector characterized by good profitability margins with medium volatility, high entry barriers, and favourable growth prospects.

Although there are a large number of players in the market, barriers to entry are high given the considerable know-how, experience, brand recognition and initial investment required to be competitive in the sector, which results in high profitability margins (EBIT margin between 13%-18%). The evolution of the hotel industry shows its link to the macroeconomic environment, which has been affected by the Covid-19 crisis in recent years, given its exposure to travel restrictions, the fall in demand and the economic slowdown. The outlook for the sector is favourable, marked by the consolidation of the recovery based on hotel indicators that continue to improve. However, we believe that the macroeconomic scenario contains certain relevant uncertainties (high inflation, high energy prices, Russia-Ukraine conflict, etc.), which could affect the overall trend.

- The hotel sector has a medium to low ESG risk exposure (sector heatmap score between 2.0 and 2.9).

The impact on the environment is considered limited given that it is not a particularly resource-intensive industry (in terms of water and land). Although the

industry may be affected by physical risks like floods, hurricanes, etc., as well as the presence in countries where access to basic services (e.g. water) may affect hotels operations. The sector may also be affected by government policies that limit leisure activity or that may have an impact on the sector, as well as by negative reviews that affect the reputation. However, this assessment has a neutral impact on the sector assessment.

Company's competitive positioning

- Despite the small size of Grupo Pestana relative to the main competitors worldwide, the group remains with a leading competitive position at a national level.

Although the group is fully concentrated in Portugal, with 82 hotels and 9,251 rooms mostly dedicated to the leisure segment (80.7% of total rooms), it is a national reference player with more than 50 years, standing out by number of hotels and rooms in Portugal. In addition, the high level of brand recognition (Pestana Hotels and Resorts, Pestana Pousadas de Portugal, Pestana Collection and Pestana CR7 "Lifestyle hotels") together with its relevant presence in tourist areas (Lisbon, Oporto, Algarve, and Madeira), unique locations (sea views), and well-balanced feeder markets (69% of total customers are from either the UK, Germany, USA, France, Spain or other countries) strengthen the overall competitive positioning. This is also reinforced by its complementary activities, such as the real estate division (10.7% of total sales), which allows the group to mitigate the impact of downturn scenarios affecting its main activity (e.g. Covid-19 crisis). All together led the group to report higher profitability margins than the sector (EBIT margin between 25%-28%).

- **Neutral ESG policy.**

In terms of ESG policies, Grupo Pestana has a neutral ESG exposure (score of 1.90). ESG issues are already considered and managed, leading to a low probability of occurrence of an ESG related impact on revenues, results, cash flows, asset value or reputation. Governance policies are strong (score of 75), marked by a qualified board of directors with separation of roles, public disclosure of policies (business code of conduct and corruption policy), and prioritization of ESG issues. This is also reinforced by good environmental metrics (score of 67) although with social metrics below average (score of 39).

Governance

- **Family ownership structure.**

The group's ownership structure remains in the hands of Mr. Dionísio Pestana, son of the founder of the group, and being involved in the business since 1976. Although the ownership structure limits the amount of financial support potentially available to the group in the event of a need arising, it does also mean stability and continuity. In addition, Grupo Pestana SGPS S.A can potentially benefit from the greater size of Pestana International Holdings S.A. The group also has a valuable portfolio of fixed assets (estimated market value of €1.0Bn) which provides additional financial flexibility.

- **Qualified management team and prudent financial policy.**

Despite the concentration of ownership and decision making, we highlight the extensive professional background of the members of the management team, which has been key in the positive performance of the company in the recent years, leading the company to its position itself as the reference player in the Portuguese market. In addition, financial policy is characterized by controlled debt levels (NFD/EBITDA below 3.0x) and strong financial autonomy (equity/TFD above 75%).

Financial Profile

Cash-flow and leverage

- **Growing and positive FFO benefited by the increase in EBITDA.**

In 2022, the group achieved an EBITDA of €128.9m (+64.4% YoY, EBITDA mg at 34.3%), favoured by the gradual lifting of restrictions (Covid-19). In regards to 9M 2023 figures, EBITDA improved to €131.7m (+15.7% vs 9M 2022, EBITDA mg at 36.2%) consolidating the recovery and even already exceeding figures reported in the full year 2019 (pre-Covid). Consequently, the capacity to generate strong and increasing cash flows from operations (FFO/EBITDA of 90.6% in 2022 and 82.9% in 9M 2023) has contributed, along with the sale of the Pestana Blue Alvor All Inclusive hotel (gain of €40m), to maintain positive FCF, €185.2m in 2022 and €85.7m in 9M 2023.

- **Low indebtedness level.**

The positive evolution of the business together with the excess of cash from the extraordinary sale of the already mentioned hotel, allowed the group to bring down the debt ratio (NFD/EBITDA) to 2.2x in 2022, from 5.3x in 2021 and 10.1x in 2020, when sales and profits were highly affected by the Covid-19 crisis, and 1.7x at the end of September 2023. The group also has good interest coverage (EBITDA/interest of 7.4x in 2022, 11.3x in September-23). In the coming years, under a favorable macroeconomic environment, debt is expected to remain low (NFD/EBITDA below 2.0x), with interest coverage (EBITDA/interest) of around 10x. This last ratio is valued favourably especially considering the current high interest rate environment (-90% of the company's debt is fixed).

Capitalization

- **Sound financial autonomy.**

The group continues to strengthen its financial autonomy, with equity equivalent to 79.5% of total financial debt in 2022 (vs 58.3% in 2021) and 108.1% at the end of September 2023, marked by the capitalization of higher results, specially in 2022 with the extraordinary profit, while maintaining debt repayments (TFD 7.7% lower in 2022 and down by a further 22.5% at September 2023). We also highlight the GAV of the company's portfolio as significant strength that reinforces its solvency (LTV of 28.5% in average).

Liquidity

- **High liquidity and a strong refinancing profile.**

Pestana Group has a good capacity to meet its commitments in the short term, supported by its ability to generate stable and recurring cash flows from its operations (FFO estimated at €152.8m in 2024) which, added to the cash and cash equivalents estimated at December 2023 (€43.6m), provide it with a good liquidity cushion to meet short-term payment obligations (€52.3m estimated at December 2023), investments and dividend payments. In addition, the company has a good refinancing profile, which is relevant in any stress scenario.

Modifiers

Controversies.

- **The company does not appear to present any controversies.**

Country Risk

- **No country risk has been identified.**

Main Financial Figures

Main financial figures. Thousands of €.						
	2019	2020	2021	2022	9M 2023 ²	22vs21%
Turnover	349,093	163,105	262,187	375,443	363,755	43.2%
EBITDA ¹	129,604	41,063	78,371	128,877	131,691	64.4%
EBITDA Margin	37.1%	25.2%	29.9%	34.3%	36.2%	4.4pp
EBIT	98,204	-7,866	46,578	133,107	99,448	185.8%
EBIT Margin	28.1%	-4.8%	17.8%	35.5%	27.3%	17.7pp
EBT	82,196	-23,482	30,950	116,121	89,791	275.2%
Total Assets	1,076,794	962,715	1,001,553	1,089,971	1,030,494	8.8%
Equity	310,749	272,440	287,036	361,157	380,564	25.8%
Total Financial Debt	503,465	470,824	492,088	454,062	351,901	-7.7%
Net Financial Debt	388,404	413,043	417,949	284,237	245,896	-32.0%
Equity/TFD	61.7%	57.9%	58.3%	79.5%	108.1%	21.2pp
NFD/EBITDA	3.0x	10.1x	5.3x	2.2x	1.7x ³	-3.1x
FFO	100,642	42,127	67,592	116,725	109,155	72.7%
FFO/NFD	25.9%	10.2%	16.2%	41.1%	44.4%	24.9pp
EBITDA/Interest	7.6x	2.6x	4.9x	7.4x	11.3x	2.6x

¹Ebitda is calculated following EthiFinance Ratings's procedures: EBIT-Gains on disposal of investments and fixed assets-reversals of losses of tangible assets- charges of depreciation and amortization- provisions. ²Unaudited accounts. ³LTM EBITDA.

Rating Sensitivity

Factors that may (individually or collectively) impact the rating:

Positive factors (↑).

- Improvement in debt levels (NFD/EBITDA below 1.2x, FFO/NFD above 65%, and EBITDA/interest above 14x in average). Increased financial autonomy (LTV below 20% in average) would also be required. An improvement on the ESG score could also benefit the overall rating.

Negative factors (↓).

- Deterioration of leverage ratios (NFD/EBITDA above 2.0x, FFO/NFD below 45% and EBITDA/interest below 8.0x in average). Decreased financial autonomy (LTV ~35%). A deterioration on the ESG score could also affect the overall rating.

Credit Rating

Credit Rating	
Business Risk Profile	BBB-
Industry risk assessment	BBB
Industry's ESG	Neutral
Competitive Positioning	BB+
Governance	BB+
Financial Risk Profile	BBB+
Cash flow and leverage	BBB+
Capitalization	A-
Company's ESG	Neutral
Anchor Rating	BBB
Modifiers	No
Rating	BBB

Regulatory Information

Sources of information

The credit rating assigned in this report has been requested by the rated entity, which has also taken part in the process. It is based on private information as well as public information. The main sources of information are:

- Annual Audit Reports.
- Corporate Website.
- Information published in the Official Bulletins.
- Rating book provided by the Company.

The information was thoroughly reviewed to ensure that it is valid and consistent, and is considered satisfactory. Nevertheless, EthiFinance Ratings assumes no responsibility for the accuracy of the information and the conclusions drawn from it.

Additional information

- The rating was carried out in accordance with Regulation (EC) N° 1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies, and in accordance with the Corporate Rating Methodology that can be consulted on <https://www.ethifinance.com/en/ratings/methodologies> and according to the Long-term Corporate Rating scale available at <https://www.ethifinance.com/en/ratings/ratingScale>.
- EthiFinance Ratings publishes data on the historical default rates of the rating categories, which are located in the central statistics repository CEREP, of the European Securities and Markets Authority (ESMA).
- In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.
- The issued credit rating has been notified to the rated entity, and has not been modified since.

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