Research Update:

Polish Development Fund ParentCo PFR S.A. 'A-' Foreign Currency And 'A' Local Currency Ratings Affirmed; Outlook Stable

June 29, 2023

Overview

- The Polish Development Fund (PFR) group is the 100% state-owned development institution that coordinates and implements development and economic support programs on behalf of the Polish government, which also guarantees PFR-issued bonds.
- We believe that PFR group would be almost certain to receive extraordinary support from the government, if needed, and we therefore equalize the group credit profile with our ratings on Poland.
- We consider PFR S.A. the group's parent company, given its direct and indirect control of the group's subsidiaries.
- We therefore affirmed our 'A-/A-2' foreign currency and 'A/A-1' local currency ratings on PFR S.A.
- The stable outlook on PFR S.A. mirrors that on Poland.

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Rating Action

On June 29, 2023, S&P Global Ratings affirmed its 'A-/A-2' long- and short-term foreign currency and 'A/A-1' long- and short-term local currency issuer credit ratings on PFR S.A. The outlook on the long-term ratings is stable.

Outlook

The stable outlook reflects our continued view that the Polish government would be almost certain to provide extraordinary support to PFR group if needed. In particular, we expect that the group will continue to play a key role in implementing the Polish government's policy priorities.

Downside scenario

We might take a negative rating action--even if the sovereign rating is unchanged--if we conclude that PFR group's policy role for, or its link with, the Polish government has weakened. This could be demonstrated by the erosion of the group's public-policy mandate, potentially reflected by a substantial contraction of its balance sheet against limited prospects for meaningful government mandates. If PFR increased its involvement (via its PFR TFI subsidiary) in managing private investor funds (for example, private pension savings)--a function that could be undertaken by private sector entities in the competitive market--this could also imply that the group's policy role had weakened. We could also consider a negative rating action if future bond issuances did not benefit from a sovereign guarantee, indicating a weaker link between PFR and the Polish government.

Upside scenario

All else being equal, we could raise the ratings on PFR if we took a positive rating action on Poland.

Rationale

We rate PFR S.A. (the parent company of the group) under our group rating methodology and criteria for government-related entities (GREs). We believe that the Polish government would be almost certain to provide timely and adequate extraordinary support to PFR group to enable its debt service, if needed, and we therefore equalize the group credit profile (GCP) with our ratings on Poland (foreign currency A-/Stable/A-2; local currency A/Stable/A-1). Our assessment of the likelihood of extraordinary support reflects our view of PFR group's:

- Integral link with the government, demonstrated by the state's 100% ultimate ownership; its regular capital injections; and explicit timely, irrevocable, and unconditional state guarantees against PFR group's bonds. The government defines and approves PFR group's long-term strategy and maintains close oversight of its activities. We also understand that PFR group holds a unique status as the state institution in charge of coordinating activities of all other development institutions in Poland; and
- Critical public-policy role for Poland as the government's prime public development institution, a role that cannot be readily undertaken by a private entity. Apart from its original mandate of catalyzing private investment, the Polish government has implemented several unique policy projects through the PFR group, including emergency support to private sector entities; promotion of the private pension savings scheme; and, as a crisis response tool, the provision of sizable financial support to the private sector amid the COVID-19 pandemic. PFR will also provide prefinancing for projects under the Recovery and Resilience Facility, where the disbursement of funds is delayed. PFR group's assets currently represent about 3% of Poland's GDP, making it one of the country's largest GREs.

We treat PFR S.A. as the group's parent given its direct and indirect control of all group subsidiaries, namely its ability to manage their strategy and cash flow. PFR S.A. concentrates over 90% of the group's capital and assets. We therefore believe that PFR S.A.'s creditworthinessis closely tied to that of the consolidated group and rate it at the same level as the GCP and ultimately the sovereign.

Ownership structure: The state fully owns PFR and guarantees it public debt

Since its establishment, PFR group's members have been joint stock companies. The government ultimately owns 100% of the group's parent PFR S.A., via direct control of 99.87% of its shares through the state treasury and a 0.13% stake via the government-owned Polish development bank. We do not expect the ownership structure to change and anticipate that PFR S.A. will remain fully state-owned.

The government appoints its representatives to the supervisory board, which in turn appoints the management board of PFR S.A. At present, a few senior government officials sit on the supervisory board. PFR S.A. is not subject to the prudential regulation of the Polish central bank.

PFR's capital group currently includes the parent company (PFR S.A.), which concentrates the majority of its capital and assets, and several subsidiaries and controlled entities. Among others, these include: PFR TFI--involved in managing specialized closed-end funds and open-end funds dedicated to Poland's Employee Capital Plan (private pension savings scheme); PFR Ventures--the fund of funds manager, providing financing via venture capital funds; PFR Nieruchomosci--the affordable housing rental construction and program manager; and PFR Portal PPK--the operator of the employee capital program related to pension reform.

We also understand that PFR S.A. is mandated by the government to coordinate other development institutions' activities, with PFR's CEO serving as the chairman of a wider association of all development institutions in Poland.

The government has provided timely, irrevocable, and unconditional budget guarantees against all debt issued by PFR S.A. since 2020 in relation to the COVID-19 support program. This debt represents over 95% of PFR's total commercial debt, with the remainder being the investment loan from the state-controlled bank (provided for the Bank Pekao stake acquisition) and the liquidity facility granted by the same bank. The sovereign guarantee is a key factor underpinning our assessment of the likelihood of support from the government. The guarantor, that is, the Polish government, shall pay the amount due on each payment date if PFR fails to fund the relevant account sufficiently on the business day preceding the respective payment date. But even before this would become necessary, the legal stipulations state that the government shall, prior to the payment date, transfer the funds needed to meet PFR's obligations.

We also understand that the government will likely continue extending guarantees for PFR S.A.'s future borrowings, including those potentially conducted to pre-finance RRF funds for Poland's development plan.

Mandate and activities: Poland's key development institution with a broad mandate for the government's critical policy priorities

Established in 2016, PFR group's core function was initially focused on fostering private sector development by direct (equity) and indirect investment across a wide range of sectors, including technology, infrastructure, and energy. Over the years, the group's mandate has broadened and now includes the following areas:

- Bridging infrastructure gaps in the Polish economy (including transport, energy, municipal, and digital infrastructure);
- Venture capital market development (direct investment and via existing private sector venture capital funds);

- Facilitating the government's pension reform by managing a long-term pension savings scheme; and
- Facilitating the implementation of Poland's recovery and resilience plan, including through pre-financing.

More broadly, however, we believe that in its current form, the group de-facto represents the government's key arm for implementing unique policy projects.

Recently, PFR has been tasked with several responsibilities in the implementation of Poland's recovery and resilience plan and administering grants from the EU's RRF (Poland is eligible for €23.9 billion [approximately 4% of GDP] of grants until 2027). PFR is providing the IT system for the implementation, for example to process payments. More importantly, and crucially to the government, is that PFR will provide bridge- and pre-financing to implement projects under the plan. Funds will stem mainly from reimbursement under the Financial Shield program, and if these are not sufficient, then from potential bond issuance. We think this role is crucial for the government because of the delays in accessing RRF funds stemming from disagreements between the European Commission and the Polish government. Given the limited timeframe for accessing RRF funds, the pre-financing via PFR could be key to the execution of various larger-scale projects.

Previously, PFR was instrumental in the execution of the government's strategy of increasing domestic ownership of the financial system by acquiring a stake in Poland's second largest bank, Bank Pekao SA, in 2016-2017, when former key shareholder UniCredit decided to exit the market. In 2019, the institution was mandated with the provision of infrastructure for the development of the private pillar of the Polish pension system. The reform introduces an auto-enrolled long-term retirement saving program managed by private sector asset managers and co-funded by the state. PFR is a public operator of the system, providing the infrastructure for financial institutions (which PFR also formally authorizes to participate) and employees/employers interested in taking part.

Furthermore, in 2020, the government used PFR group, via parent company PFR S.A., as its prime tool to mitigate the economic fallout from the COVID-19 pandemic under the Financial Shield stimulus program. PFR S.A. has provided partially nonrepayable liquidity loans for micro, small and midsize, and large firms of over Polish zloty (PLN) 73 billion (over 2% of GDP). The program was funded by PFR S.A.-issued bonds that are fully guaranteed by the government.

We believe that the size and the type of projects the institution has been historically implementing render it almost irreplaceable by any other GRE or private sector entity. Although the COVID-19-related program will continue to be gradually unwound in the coming years, it underlines the importance of PFR group as a response tool for future crises, in addition to its mandates to implement critical policy programs.

Track record of support: Regular capital injections amid additional channels of government support

The government made several equity injections into PFR group in the past few years. By year-end 2022, shareholders' equity had reached PLN12.3 billion, compared with PLN2.8 billion in 2019. We understand the government is planning to inject further capital to support the fund's activities in the future.

Apart from capital support and state guarantees, other channels of potential extraordinary support include the exemption of PFR from dividend payments to the budget, lending from other state-owned and controlled financial institutions.

Because we equalize the GCP with that on the sovereign, we do not consider the group stand-alone credit profile to be a rating driver. This reflects our view that the government is almost certain to provide extraordinary support to service debt, and we currently do not consider this support as subject to transition risk.

The institution's funding base comprises shareholders' equity, interbank loans, and bonds issued under the pandemic-related stimulus program. The debt repayment profile is relatively heavy, with over 65% of the bonds coming due in 2024-2025. We understand that the government will support PFR to fulfill its obligations on time and in full by explicitly budgeting for corresponding subsidies in its annual budget and channeling them to the institution ahead of debt maturities.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- General Criteria: Group Rating Methodology , July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions , March 25, 2015
- General Criteria: Principles Of Credit Ratings , Feb. 16, 2011

Related Research

- Poland, June 26, 2023

Ratings List

Ratings Affirmed	
Polish Development Fund (PFR S.A.)	
Issuer Credit Rating	
Foreign Currency	A-/Stable/A-2
Local Currency	A/Stable/A-1