Polish Development Fund (PFR S.A.)

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This report does not constitute a rating action.

Credit Highlights

Overview

Key strengths	Key risks
Almost certain likelihood of extraordinary government support from the sole ultimate owner, the Polish government.	Exposure to changes in government policy.
Critical role as a government tool for unique policy projects.	Uncertain exit strategy from some government-spurred investments.
Explicit state guarantees against all bonded debt.	

The fully-state owned Polish Development Fund (PFR) acts as a government tool for major policy projects. On top of serving as a key channel of the Polish government's fiscal response to the COVID-19 pandemic, starting this year PFR will conduct a new policy objective of administering grants allocated to Poland from the EU's post-pandemic Recovery and Resilience Facility (RRF). Poland is eligible for a sizable €23.9 billion (4.3% of 2021 GDP) of grants until 2027, with the PFR set to maintain the liquidity of grant-financed projects via bridge financing.

S&P Global Ratings considers the credit quality of PFR group and its parent PFR S.A. as equal to that of the sovereign. All PFR's bonds are guaranteed by the Polish government and there is close government oversight of the institution's activities. There is also a strong track-record of capital injections from the state to PFR. Together with its major public policy role, these factors allow as to believe there is an almost certain likelihood that the state would provide timely and sufficient support to PFR in the event of stress.

Outlook

The stable outlook reflects our view that the likelihood of extraordinary support by the Polish government for PFR group will remain almost certain. In particular, we expect that the group will obtain further public policy responsibilities as the COVID-19 pandemic and the government's fiscal response recedes.

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 and/or its link with the Polish government has weakened. For example, this could be signaled by the erosion of the group's public-policy mandate, perhaps reflected by the more rapid contraction of its balance sheet than we currently expect on the back of only moderate growth of the EU RRF's related lending against the phase-out of the COVID-19-focused programs. Another scenario that could suggest weakening policy role could be PFR's increased involvement (via its PFR TFI subsidiary) in managing private investor funds (such as private pension savings)--a function that could be undertaken by private sector entities in the competitive market.

Upside scenario

A positive rating action would be subject to an equivalent action on Poland.

Rationale

We rate PFR S.A. (parent company of the group) under our group rating methodology and criteria for government-related entities (GREs). We believe that the institution de-facto represents the Polish government's key agency for implementing unique policy projects. We believe that there is an almost certain likelihood that the Polish government would provide timely and adequate extraordinary support to PFR group to enable its debt service, if needed, and 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 to 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 bonded debt. The government defines and approves PFR group's long-term strategy and maintains close oversight of its activities. We also understand that PFR group is the state institution in charge of coordinating the 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, PFR group has been used by the government to implement several major policy projects, including emergency support to private sector entities, promotion of the private pension savings scheme, the provision of financial support to the private sector amid the COVID-19 pandemic, and the administration of the EU RRF's grants. PFR group's assets currently represent about 3.4% 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 direct their strategy and hold their cash flow. PFR S.A. concentrates over 90% of the group's capital and assets. We therefore believe that the creditworthiness of PFR S.A. is closely tied to that of the consolidated group and rate it at the level of the GCP and ultimately the sovereign.

Mandate and activities: Poland's development institution with a broad mandate in critical policy areas

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, 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
- Fostering investment in affordable housing and developing the housing rental market.

More broadly, however, we believe that in its current form the group represents the Polish government's arm for implementing unique policy projects. For example, the institution was instrumental in increasing domestic ownership of the financial system by acquiring a stake in Poland's second largest bank, Bank Pekao S.A., 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.

In 2020, the government used PFR group, via parent company PFR S.A., as its tool to mitigate the economic fallout from the COVID-19 pandemic under the Financial Shield fiscal stimulus program. This has increased the institution's balance sheet multifold. Over 2020-2022, PFR S.A. has provided partially nonrepayable liquidity loans for micro, small and midsize, and large firms of over Polish zloty (PLN) 63 billion (3% of GDP), with some parts transformed into grants as recipients met certain criteria, such as job retention. The program has been funded by PFR S.A.-issued bonds, guaranteed by the government.

The COVID-19-related program will gradually unwind in the coming years as loans are repaid or written-off. However, we do not expect this to erode PFR’s government policy role. This is because in 2022 the institution was mandated with the new function of administering grants allocated from the EU's RRF. Poland is eligible for €23.9 billion (4.3% of 2021 GDP) of grants until 2027. PFR will channel the RRF grants to preselected domestic projects and cover potential liquidity gaps during their execution. To finance the latter, we understand that PFR will use its free liquidity or issue sovereign-guaranteed bonds.

We believe that the size and the type of projects the institution has been historically implementing make it almost irreplaceable by any other GRE or private sector entity.

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 99.9% of its shares through the state treasury and a 0.1% stake via the government-owned Polish development bank (BGK). We do not expect the ownership structure to change and anticipate that PFR S.A. will remain 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 the pension reform.

We also understand that PFR S.A. is mandated by the government to coordinate the activities of other development institutions, 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. We also understand that the government will likely continue extending guarantees for PFR S.A.'s future borrowings, including those conducted under the RRF grants’ administration function.

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 2021, shareholders' equity increased multiple times to about PLN12.9 billion, compared with PLN 2.8 billion in 2019. We understand the government is willing to make further injections 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, and 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 likelihood of extraordinary government support to service debt is almost certain, and we currently do not consider this support 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 continue supporting PFR to fulfill its obligations on time and in full by explicitly accounting for corresponding subsidies in its annual budget and channeling them to the institution ahead of debt maturities.

Related Criteria

- 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

- Sovereign Risk Indicators, April 11, 2022. An interactive version can be found at www.spratings.com/SRI

Ratings Detail (as of June 29, 2022)*

Polish Development Fund (PFR S.A.)		
Issuer Credit Rating		
Foreign Currency		A-/Stable/A-2
Local Currency		A/Stable/A-1
Issuer Credit Ratings History		
23-Jun-2021	*Foreign Currency*	A-/Stable/A-2
23-Jun-2021	*Local Currency*	A/Stable/A-1
Sovereign Rating		
Poland		
Foreign Currency		A-/Stable/A-2
Local Currency		A/Stable/A-1

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*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.