

State Development Bank of Poland (BGK)

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	Issuer Rating	Outlook
Moody's	-	-
S&P	-	-
Fitch	A-	Stable

Source: Moody's, S&P and Fitch;

Background

Bank Gospodarstwa Krajowego (BGK) is the state development bank of Poland, the only institution of its kind in the country. BGK was initially established in 1924 and resumed activities in 1989 following the collapse of Communist rule. BGK's mission is to support social development and economic growth in Poland and provide financial services on behalf of the public sector. It is supervised by the Ministry of Economic Development and overseen by the national financial supervisory authority (UKNF). BGK is rated 'A-/F1/Stable' by Fitch, in line with Poland's sovereign rating.

The development bank supports investment, especially long-term projects, in both the private and the public sector. BGK also played a key role in the Polish government's response to the Coronavirus pandemic, managing a fund for which it issued state-backed bonds amounting to PLN144bn or 5.5% of 2021 Polish GDP by 1H22. In December 2020, BGK was officially accredited by the European Commission (EC) to become an implementation partner for projects that benefit from EU funds, including those with respect to urban and regional development, digitisation, energy efficiency and renewable energy.

Main activities

BGK contributes to the implementation of the state's economic objectives, providing funding for SMEs, infrastructure investments, housing, energy efficiency and public utilities.

SME support: BGK manages several special purpose funds and a number of government programmes, including the provision of loans and guarantees to SMEs. BGK also co-operates with the European Investment Bank (EIB) in supporting SMEs by providing portfolio guarantees to commercial banks. These are counter-guaranteed by the European Investment Fund's 'Competitiveness of Enterprises and Small and Medium-sized Enterprises' (COSME) programme. BGK also oversees the implementation of the government's export-support programme, which benefits Polish SMEs as well as larger enterprises.

Infrastructure, municipalities and housing: Financing of infrastructure projects is conducted via dedicated funds, such as the national road fund or the national railway fund, which make an important contribution to the domestic economy. The bank also supports the financing of municipalities, related companies, and social housing. BGK also plays a role in public finance management to increase efficiency in the public sector. In 2022 BGK was named administrator of two newly established funds, the aid fund and armed forces support fund, which further underline the institution's importance in implementing government policy.

BGK – Key Data*		
PLNm - Balance Sheet	FY21	FY20
Total assets	196,644	160,326
Customer loans outstanding	33,263	33,452
Securities	93,975	76,902
Customer deposits	150,804	116,138
Debt securities issued	3,860	4,859
Total equity	24,722	23,924
PLNm – P&L	FY21	FY20
Total income	1,897	1,598
<i>Net interest income</i>	1,034	955
<i>Net fee & commission income</i>	294	248
Total expenses	-725	-742
Loan Loss Provisions	-332	-385
Net income before tax	1,093	447
Net income after tax	875	367

Source: Investor Reports; *1 EUR = 4.75 PLN as of 22.08.2022

2021-2025 Strategy

The 2021–2025 strategy aims to strengthen the position of the bank and the Polish economy in international markets by supporting the social and economic development of the country and ensuring that relevant funding reaches the banking sector. The new strategy was also developed in response to the changing economic environment, taking into account societal, technological and regulatory developments. It was therefore supplemented with an additional objective related to sustainable development. BGK states that it wants to become a leading institution in sustainable development programmes. Key objectives are defined by three external pillars:

- **Sustainable development**, where the ambition is to support the socio-economic development of the country at least so as not to deteriorate living conditions for future generations;
- **Social commitment**, through the development of social capital in the areas of education, culture, sport and ecology;

- **International business and cooperation**, aimed at improving the competitiveness of the Polish economy by increasing the international orientation of Polish enterprises and building awareness of Poland's attractiveness among foreign investors as a country with high intellectual capital;

The above is complemented by two internal pillars aimed at maximising the efficiency of activities in the business pillars:

- **Digital and process transformation**, creating better conditions for a dynamic environment via improved processes and digitalisation;
- **Effective management model**, ensuring a growing scale of tasks completed with a view to meeting the increasingly complex needs of the rising number of stakeholders.

Eight dedicated programmes support the implementation of the strategic pillars and define the scope of the bank's operations. Over the course of the previous 2017-2020 strategy, BGK's balance sheet grew to PLN160bn (+24.4% CAGR), financing PLN8.4bn of exports and foreign expansion of Polish companies. BGK states that the economic value it created through the funding it provided was PLN168bn.

Financial strength indicators

Profitability – BGK has been consistently profitable over the past ten years. However, it has displayed a degree of volatility in its bottom-line, likely due to its large securities holdings. In FY21, the bank reported consolidated group net income of PLN875m, up significantly from PLN367m the year before. The strong result was only partially driven by top-line revenues items such as higher NII at PLN1bn (+8.3% yoy) and net fee and commission income at PLN294m (+18.7% yoy). Most of the increase comes from other operating income items that do not directly relate to banking operations. These can stem from a variety of sources such as positive fair value adjustments on investments, recovered bad debt, release of provisions for litigation and legal claims or the sale of fixed assets. As at FY21 other operating income items stood at PLN332m (+138.8% yoy). Bottom line results also benefitted from slightly lower loan loss provisions of PLN332m (-13.6% yoy) but they remained elevated compared to levels observed between 2017 and 2019.

Asset quality – At end-2021, BGK had total consolidated assets of PLN197bn (+22.6% yoy). The balance sheet grew mostly on the back of higher cash and equivalents with the central bank (+PLN16bn) and a larger securities portfolio (+PLN16bn). The three largest balance sheet items are securities (48% of total), cash and balances (25%) and loans and advances to customers (17%). BGK makes disclosures around concentration risk that highlight a degree of customer as well as sector concentration. At FY21, the top 20 single entity non-bank customers accounted for 71.9% of the loan portfolio (FY20: 66.8%). When looking at groups of associated clients, the five largest accounted for 51.1% exposure in the loan portfolio (FY20: 44.3%). Sector concentration is monitored on a daily basis pursuant to internal procedures for industry limits. The top three sector concentrations relate to public administration and defence, compulsory social security (24.8%), mining and quarrying (12.7%) and the production and supply of electricity, gas and steam (10.6%). Credit risk by currency is mostly limited to Polish Zloty (84.8%) followed by Euro (10.2%) and US Dollar (4.8%), broadly similar to last year.

Funding & Liquidity - As of end-2021, BGK's total non-equity funding stood at PLN172bn and primarily consists of corporate and public-sector deposits (88% of total), repurchase agreements (6%), interbank lending (2%) and debt issuance (2%). Deposit and derivative services at the request of the ministry of finance (MoF) tend to be large but can be volatile. Debt is issued out of its senior unsecured bond programme that permits issuance up to PLN10bn, while its liquidity position is comfortable as measured by LCR and NSFR both at 173% as of end-2021. The solid liquidity indicators provide some comfort with regards to balance sheet concentration and volatility. BGK's debt is not explicitly guaranteed by the Polish government but by law the state is required to provide BGK with sufficient funds and liquidity to ensure the fulfilment of its responsibilities, which we consider to represent implicit support.

ESG considerations

BGK's 2021–2025 strategy includes pillars on sustainable development and social commitment, the specific provisions of which account for ESG dimensions. Early forays into sustainable finance occurred last year when BGK, together with Bank Pekao, granted financing for a PLN496m bond issue programme to support the modernisation of tram networks, broadening the fleet of zero-emission vehicles. BGK appears to not have developed its own sustainable funding programme yet but it has stated that it has begun work with a consulting firm under a grant awarded by the European Commission to prepare for green finance. In 2022, BGK also plans to prepare guidelines and concepts for sustainable procurement which will account for ESG certificates, among other things. BGK stated that when making purchasing decisions with business partners it will prefer those that have appropriate environmental certificates.

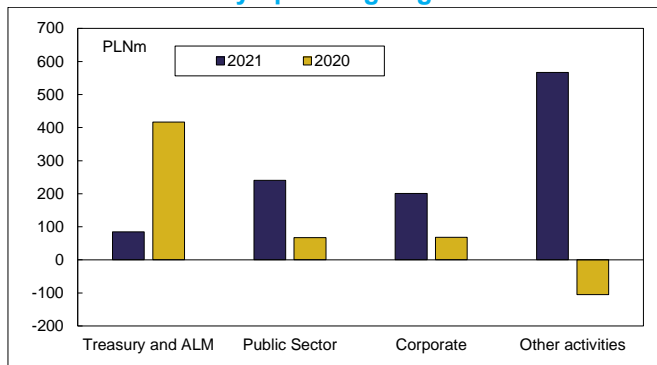
Capitalisation – The bank's capitalisation at FY21 was solid, with a CET1 ratio of 28.4% (FY20: 33.9%). The decline against last year's levels was predominantly driven by RWA inflation. However, this occurred in line with the balance

sheet expansion, reflected in the stable RWA density (RWA/Total Assets), while nominal capital amounts remained almost unchanged. According to the bank's FY21 Pillar III report, BGK is exempt from EU capital legislation such as the Capital Requirements Directive (CRD) IV or the Bank Recovery and Resolution Directive (BRRD) but it remains subject to banking supervision by UKNF.

Rating agencies' views

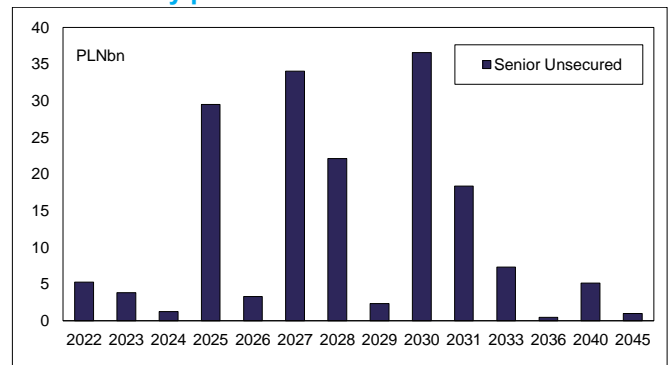
Fitch – In August 2022, Fitch affirmed the ratings of Bank Gospodarstwa Krajowego's (BGK) Long-Term Foreign Currency Issuer Default Rating (IDR) at 'A-' with a Stable Outlook. BGK's ratings reflect Fitch's view of an extremely high probability of support from the Polish state (A-/Stable) if needed. BGK's IDRs, senior debt rating and Government Support Rating (GSR) are equalised with the Polish sovereign's ratings. This is primarily based on BGK's policy role, which is underpinned by 100% state ownership. The Stable Outlook on the bank's Long-Term IDR mirrors that on the Polish sovereign rating. BGK's Short-Term IDR of 'F1' is equalised with that of the Polish sovereign.

Profit before tax by operating segments



Source: Company reports

Debt maturity profile



Source: Company reports; Bloomberg; as of 16.08.2022

Recent Benchmark Transactions

Issue Date	Security	Maturity/Call	Currency	Size (m)	Coupon	Yield	Final Spread (bps)
31/05/2022	Sr. Unsecured	7Y	EUR	500	3.0%	3.094%	MS + 155
05/05/2022	Sr. Unsecured	5Y	EUR	100	1.625%	1.720%	MS + 45
28/10/2021	Sr. Unsecured	4Y	USD	400	1.750%	n.a.	T + 86
13/10/2021	Sr. Unsecured	7Y	EUR	500	0.375%	0.432%	MS + 45
08/07/2021	Sr. Unsecured	10Y	EUR	500	0.50%	0.607%	MS + 50

Source: Bloomberg

This is an issuer profile and contains factual statements only. All statements are sourced from the issuer's financial reports, which can be found at <https://www.en.bgk.pl/about-us/>

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- 2: Outperform TOPIX/benchmark index by 5-15% over the next 12 months.
- 3: Out/underperform TOPIX/benchmark index by less than 5% over the next 12 months.
- 4: Underperform TOPIX/benchmark index by 5-15% over the next 12 months.
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- In addition to the purchase price of a financial instrument, our company will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥2 million per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements**.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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