MFB Hungarian Development Bank

Rating Report

Foreign currency

Long-term issuer rating/Outlook

BBB/Stable

Senior unsecured debt

BBB/Stable

Short-term issuer rating/Outlook

S-2/Stable

Local currency

Long-term issuer rating/Outlook

BBB/Stable

Senior unsecured debt

BBB/Stable

Short-term issuer rating/Outlook

S-2/Stable

Rating rationale and Outlook

The BBB rating of MFB Hungarian Development Bank Private Limited Company (MFB) reflects the statutory funding guarantee of Hungary (BBB/Stable) for MFB's financial obligations arising from bonds issued, credits and loans taken, deposits from the interbank market and replacement costs of currency or interest rate swaps for fundraising purposes.

In addition, Scope acknowledges i) a record of financial support from Hungary, which has strengthened MFB's capitalisation and liquidity via multiple capital increases in recent years; ii) the supportive legal framework defining MFB's strong cohesion with Hungary, making any changes to the bank's business model unlikely; and iii) MFB's high strategic importance to the sovereign as a key government-related entity (GRE) delivering competition-neutral services, with a unique policy function in the country.

The bank benefits from a robust balance sheet with sound capitalisation and asset quality. MFB's modest profitability alongside limited loan portfolio diversification reflects the development bank's public policy mandate.

Figure 1: Scope's approach to rating MFB

MFB Hungarian Development Bank		
Public Sector	**Hungary (BBB/Stable)**	
Step 1: Integration with the public sponsor (QS1)	Rating approach	Top-down
Step 2: Top-down approach (QS2)	Rating distance to the public sponsor	0 notches (BBB)
Step 3: Equalisation factor	Rating equalisation with public sponsor?	Yes (BBB)
Final rating	**BBB/Stable**	

Source: Scope Ratings

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Credit strengths and challenges

Credit strengths	Credit challenges
• Funding guarantee from the Hungarian state • Supportive legal framework, record of financial support • Strategic policy role • Sound asset quality • Robust capitalisation	• Modest profitability • Limited loan portfolio diversification

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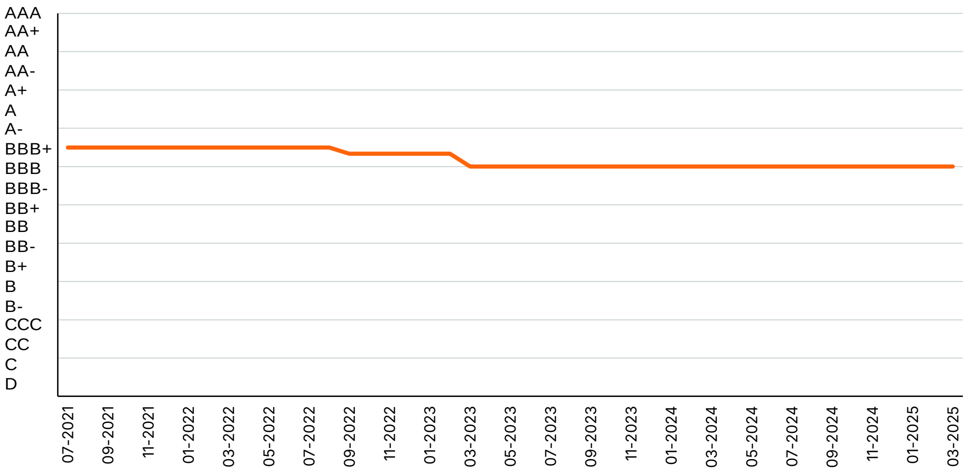
Rating Outlook and Sensitivities

The Stable Outlook is aligned with the Stable Outlook on the sovereign rating of Hungary and reflects our assessment that risks are balanced.

Positive rating divers	Negative rating drivers
• A positive change in Hungary's sovereign rating/Outlook	• A negative change in Hungary's sovereign rating/Outlook • Changes to the legal framework or guarantee structure, notably weakening government support

Figure 2: Rating history[1]



[1] Foreign-currency long-term issuer rating. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment. Source: Scope Ratings.

Integration with Hungary

Legal status and shareholder structure

Wholly owned by Hungary with activities defined by legal act

MFB is an entity created under public law, with the legal status, tasks and activities of the bank defined by Act XX of 2001 (MFB Act), which entails close central government oversight over MFB's activities. Hungary is the bank's sole owner and legal acts define exclusive state ownership. The Bank Recovery and Resolution Directive does not apply to MFB.

Purpose, activity and financial interdependencies

Key government -related entity as development bank

MFB is the only development bank in Hungary focused on the domestic market, with total assets of HUF 3,541bn at YE 2023 on a stand-alone basis (around EUR 9bn, or around 5% of Hungarian GDP). MFB is instrumental to the state and is governed by the MFB Act, which defines the mandate and strong cohesion with the sovereign.

The bank operates within the national economy. Its mandate is to support infrastructure development, finance key state and municipal investments and provide complementary financing to SMEs. This allows MFB to avoid competition with commercial financial institutions. MFB contributes to economic development as the government's key vehicle to mobilise and intermediate EU funds on behalf of local and national managing authorities.

Control and regular support

Extensive ownership control, financial support

The Hungarian state exerts proprietary control over MFB's activities as their scope and content are defined by a comprehensive legal mandate.

Financial support was provided by the Hungarian state on multiple occasions, with latest capital increases in 2022 in the context of the bank's policy-related business growth and anticipated increase in risk-weighted assets.

Likelihood of exceptional support

Guarantees ensure timely support

The explicit, direct and irrevocable statutory funding guarantees provided by the Hungarian state for MFB's financial obligations ensure timely financial support for MFB. MFB's key strategic purpose, low substitution risk and contribution to macro-economic stability support a high likelihood of exceptional support for MFB from the Hungarian state if ever needed.

Rating equalisation with Hungary

MFB's ratings are equalised with the Hungarian sovereign rating

MFB benefits from established, multi-layered and explicit liability support provided by Hungary. The MFB Act requires the Hungarian state to provide statutory guarantees for bonds issued by MFB, credits and loans taken, deposits collected from the interbank market, and replacement costs of currency and interest rate swaps entered into by MFB for fundraising purposes.

The MFB Act stipulates that MFB cannot incur guaranteed liabilities beyond the limits approved in Hungary's annual central budget. As Hungarian law requires explicit, direct and irrevocable guarantees for MFB's payment obligations in connection with its fundraising, only a parliamentary act can amend, revoke or restrict these guarantees. Once an act is effective, the amended, revoked or restricted guarantees only apply to future transactions. We deem this scenario unlikely.

The Hungarian state sets annual guarantee limits via budgetary acts. Debt is debited from the budgetary limit on the transaction date. This calculation method serves budgetary purposes only, ensuring exchange rate fluctuations have no effect on the guarantees' enforceability. The budgetary limit of the repayment guarantee was HUF 4,300bn in 2024 (utilisation YE: 65%). The 2025 central budget of Hungary set the budgetary limit of the repayment guarantee at HUF 5,000bn.

MFB further benefits from foreign exchange arrangements that allow the bank to manage foreign exchange risk. The arrangements with the ministry responsible for state finances (currently the Ministry for National Economy) are connected to certain loan programmes based on government resolutions and relate to deposits accepted, credits and loans taken, bonds issued, and replacement costs of foreign exchange swaps entered into for fundraising purposes. The bank's exchange rate risks are assumed by the central government's budget up to a threshold, via hedging agreements based on the forint equivalent of the euro funds. The state reimburses MFB for losses incurred in converting loans or funds into euros; foreign exchange gains are passed on to the state budget. The main objective of this scheme is to ensure that interest rates remain low for the ultimate beneficiaries of MFB's loans. At the same time, the scheme shields the bank from potential losses arising from forint volatility.

FX risks managed via mechanism with government

On a case-by-case basis and via government resolutions, the Hungarian state guarantees payment obligations arising vis-à-vis MFB or an intermediary financial institution from credits, loans and explicit, direct and irrevocable guarantees and other undertakings granted directly or via an intermediary (back-to-back guarantee). For some loan programmes, the Hungarian state provides a liability and/or asset side interest rate subsidy for certain credits and loans provided by MFB at its own risk.

Standalone fundamentals

The development bank's public policy mandate is reflected in its modest profitability. MFB's capitalisation with a CET1 ratio of 16.2% at YE 2023 is adequate and benefits from capital injections in recent years, mitigating a substantial increase in risk-weighted assets due to the bank's expanded activities since 2020. The bank's asset quality is robust, with low NPLs and comprehensive portfolio protection, including via guarantees from the public sponsor and other credit enhancements. The statutory guarantees provided by the Hungarian state on MFB's payment obligations regarding funding activities ensure access to favourable refinancing conditions. Following recent capital contributions by the Hungarian state, MFB's capitalisation provides sufficient room for future growth.

Public policy mandate drives standalone fundamentals

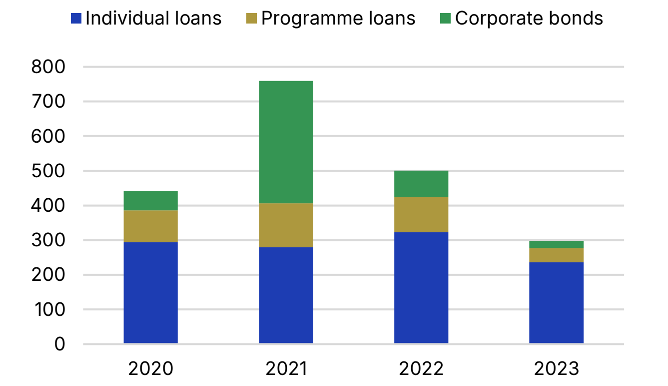
Business model and strategy

MFB's activities are split into four areas: i) lending via disbursements under loan programmes or individual loans and guarantees mostly for large corporates, SMEs, agricultural businesses and municipalities; ii) fundraising activities; iii) equity participations; and iv) intermediation of EU funds, which is off-balance-sheet as funds are distributed on behalf of managing authorities. In addition to development banking activities, the bank holds a conservatively managed liquidity portfolio that includes cash, central bank deposits and securities.

MFB operates along four main activities

Figure 3: Business volumes

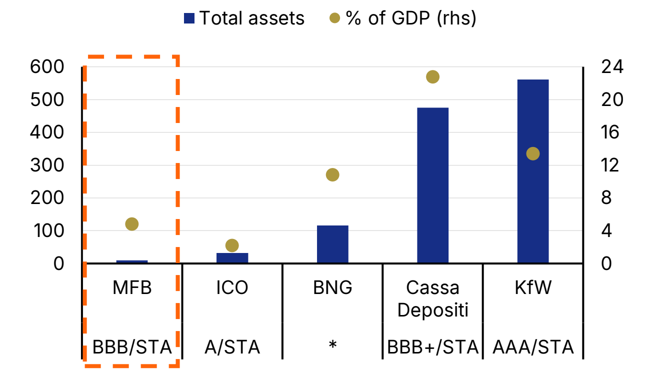
HUF bn, loans approved and bonds subscribed



Source: MFB, Scope Ratings

Figure 4: Total assets versus selected peers

EUR bn (YE 2023), % (rhs)



Note: * BNG rating available on subscription. Source: SNL, Scope Ratings

Due to elevated activity in support of economic activity in Hungary during Covid-19 and the war in Ukraine, MFB's balance sheet size roughly doubled between 2019 and 2022 to around HUF 2,970bn at YE 2022. Business volumes declined in 2023, due to elevated interest rates in Hungary as well as a recessionary economic environment. The bank approved HUF 236bn in individual loans, HUF 41bn via loan programmes and subscribed to HUF 21bn in corporate bonds (**Figure 3**, previous page).

In the medium-term strategy 2022-2030, MFB targets new commitments of HUF 1,600bn up to 2025 and a further HUF 3,600bn from 2025 to 2030. The 2025 target was met by YE 2023, highlighting high demand for the bank's products given Hungary's structural funding gap for SMEs.

Profitability and capitalisation

Modest profitability as a consequence of public policy mandate

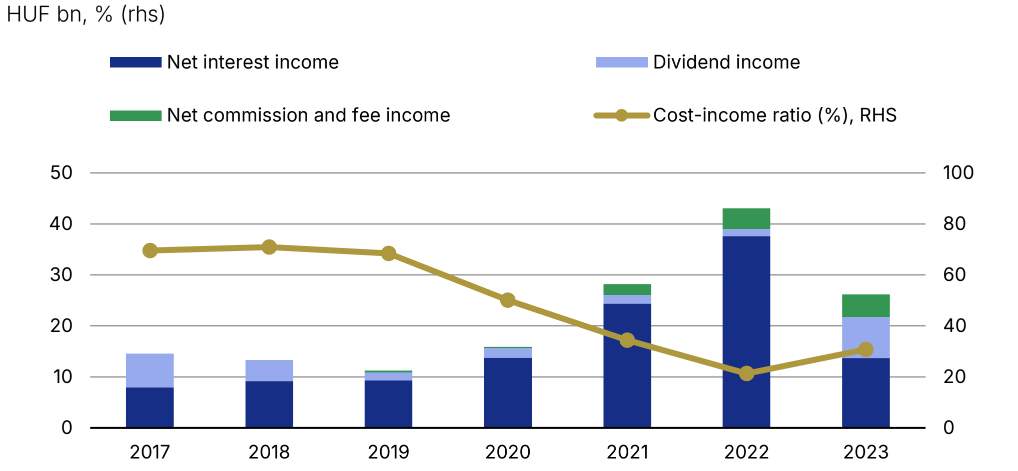
MFB's development banking activities are reflected in its moderate profitability, with return on equity averaging 1.23% over the past five years.

Net income on a stand-alone basis declined to HUF 2.4bn in 2023 from HUF 6.2bn in 2022, due to lower net interest income, declining sharply to HUF 13.7bn from HUF 37.6bn mainly due to higher interest expenses on new borrowings. MFB's net interest income relative to total assets has been around 0.8% over the past five years. Net fee and commission income was broadly stable, which related mostly to the bank's guarantee portfolio, while dividend income rose to HUF 8bn, from HUF 1.4bn in 2022.

Relatively high impairment charges in 2022/23 driven by economic environment

Expenses on banking operations increased by 9.7% in 2023. Impairment charges remained relatively elevated at HUF 21.9bn, down from HUF 26.7bn in 2022, due to the adverse domestic macroeconomic environment. Finally, MFB continued to invest in IT infrastructure. The bank's cost-to-income ratio was relatively low at 30.8% in 2023, mainly driven by higher earnings.

Figure 5: Revenue components and cost-to-income ratio

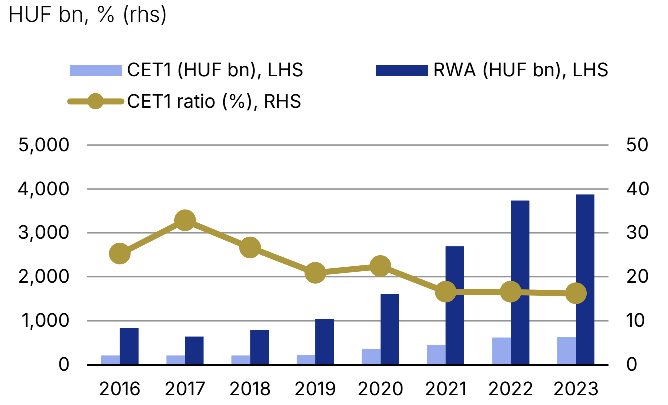


Source: MFB, Scope Ratings

History of capital injections underpin comfortable CET1 ratio

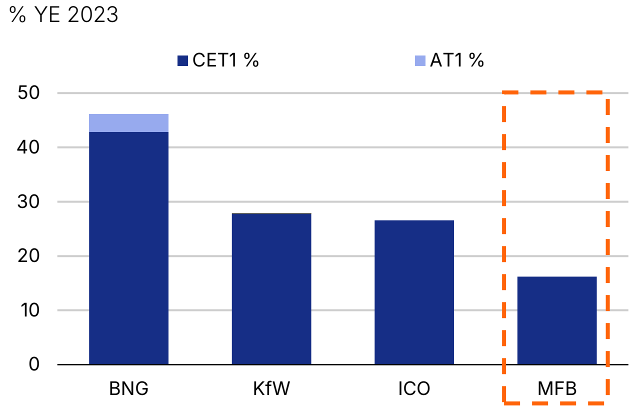
In the context of increasing risk-weighted assets and limited internal capital generation, the bank has received multiple precautionary capital increases from the Hungarian state in recent years. In 2022, the Bank received a total of HUF 170bn in capital contributions, with the capital increase serving the fulfilment of an increasing number of tasks. CET1 capital stood at HUF 627bn in 2023 against risk-weighted assets of HUF 3,872bn, with a corresponding CET1 ratio of 16.2%.

Figure 6: CET1 ratio



Source: MFB, Scope Ratings

Figure 7: Capitalisation versus selected peers



Source: SNL, Scope Ratings

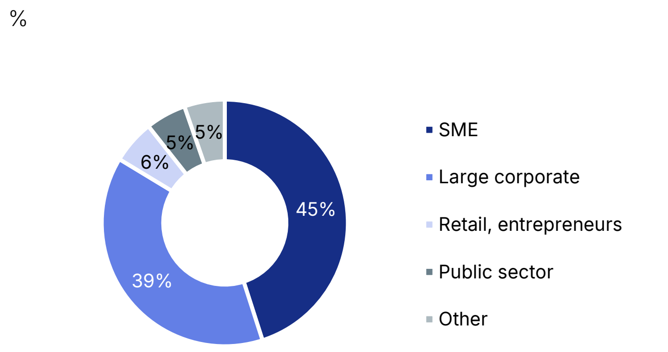
Portfolio risk and asset quality

Portfolio concentrated on large corporates and SMEs in Hungary

MFB's exposure is concentrated on SMEs (45.0% of the total portfolio in 2023), large corporates (38.6%) and the public sector (5.3%) (**Figure 8**). The bank's loans are all in Hungary, creating geographical concentration in line with the bank's domestic policy mandate.

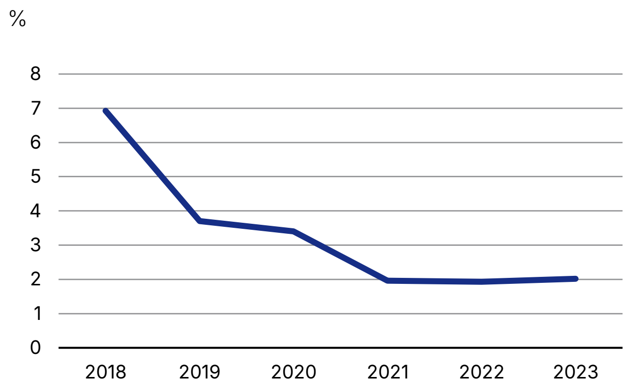
MFB's loan book shows a strong asset quality and low non-performing exposure. The share of non-performing loans relative to gross customer loans has been stable in recent years at around 2%. The sizeable loan programmes launched in 2020 against the Covid-19 pandemic continue to support MFB's balance sheet with limited risk given state guarantees covering up to 90% of associated credit risk.

Figure 8: Lending portfolio per customer group



Source: MFB, Scope Ratings

Figure 9: Non-performing loans (NPL) ratio



Source: MFB, Scope Ratings

Funding and liquidity

Well-established funding profile underpinned by guarantee

MFB benefits from an established access to international capital and money markets, high liquidity in the domestic financial sector and internal liquidity buffers. MFB funds its operations i) by issuing debt securities, ii) by taking bilateral and club loans from the domestic and international loan market and iii) via facilities from multilateral development banks. Bank loans are partly provided by supranational lenders and promotional banks, including the European Investment Bank (EIB, AAA/Stable) and Council of Europe Development Bank (CEB, AAA/Stable) and are tied to long-term lending programmes.

The bank's debt obligations benefit from preferential regulatory treatment thanks to the explicit liability support provided by Hungary, which implies a risk weight of 0% for forint-denominated issues and 50% for euro issues, according to the standardised approach of Basel III/CRR.

Well-diversified funding mix

As of YE 2024, the share of liabilities denominated in HUF was 47.6%, 36.7% was in euros and 15.7% in USD. In 2023, MFB issued its first international USD bond in ten years with a five year and one month maturity and a principal of USD 1.125bn, marking the largest-ever transaction for the bank. MFB's funding strategy foresees a strategic presence on the domestic HUF bond market.

Liquidity reserve underpins liquidity

MFB's liquidity portfolio amounted to around HUF 519bn (14.7% of total assets) at YE 2023. In addition to funds held at the central bank, MFB holds Hungarian government securities, bank deposits and securities other than Hungarian government securities eligible as central bank collateral. MFB is exempt from Basel liquidity requirements via the MDB Act.

Environmental, Social and Governance Factors (ESG)

ESG factors within MFB's legal framework, policy mandate and mid-term strategy

Material ESG factors are captured by Scope's rating approach through several analytical areas.

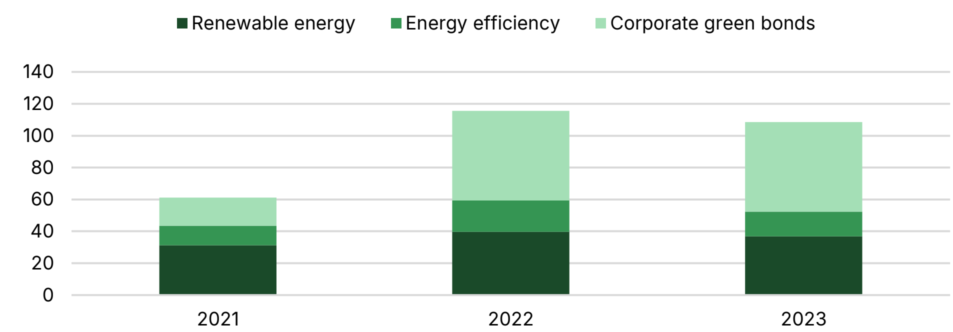
Governance and social considerations are material to MFB's credit rating and were included in the assessment of the level of integration with the public sponsor, highlighting the supportive legal framework that mandates MFB's compliance with its statutes and underscores its role as a competition-neutral public law entity. MFB's role encompasses the provision of key services that serve national economic and social objectives. Our governance assessment also considers MFB's standalone fundamentals, highlighting its sound risk profile and risk management.

Environmental considerations include the bank's role in fostering the public sponsor's transition agenda, with MFB integrating sustainability into its mid-term strategy 2022-2030. In its sustainable finance framework, the bank commits to contributing to the United Nations SDGs and the Paris Agreement, as well as EU environmental objectives in its lending activities.

Sustainable lending programmes include renewable energy and green buildings, and SME and higher education projects. In 2024, MFB introduced a Corporate Energy Efficiency Loan Programme in cooperation with the EIB and CEB. MFB established a sustainable finance framework in 2023 and issued its first green and social bonds in the first half of 2024.

Figure 10: Stock of individual loans supporting environmental objectives

HUF bn



Source: MFB, Scope Ratings

Appendix I. Qualitative Scorecards

Qualitative Scorecard 1: Integration with Hungary (BBB/Stable) and Rating Approach

Analytical component (weight)	Assessment (Score)	Analytical rationale
Legal status (40%)	Medium (50)	MFB Zrt. (Private limited company) has a private legal form and implies that the bank could be subject to private insolvency proceedings. But unlike other banks with a private legal form, MFB is an entity created under public law, with the legal status, tasks and activities of the bank defined by Act XX of 2001 (MFB Act), which entails close central government oversight over MFB's activities.
Purpose & activities (20%)	High (100)	As a development bank, MFB has as its main objective addressing shortcomings in the financial market. It provides funding opportunities to businesses in areas where commercial banks cannot provide financing efficiently, including preferential loans to businesses, carrying out fund management and providing other financial services within the framework of its mission. It is in operation since 1993.
Shareholder structure (20%)	High (100)	Fully state-owned.
Financial interdependencies (20%)	High (100)	MFB is tasked with distribution of EU funds which involves providing financial support to Hungarian state-affiliated public entities.
Approach adopted		**Top-Down**

Source: Scope Ratings

Qualitative Scorecard 2: Indicative notching vis-a-vis Hungary

Analytical component (weight)		Assessment	Analytical rationale
Control and regular support	Strategic and operational decision making	High (100)	MFB's organisation, functioning and tasks are almost fully legislation based. The MFB Act sets out the rules for the bank's operations.
	Key personnel, governing & oversight bodies	High (100)	Certain laws enable the Hungarian state to alter MFB's strategy and mandate and to appoint and dismiss key personnel including members of governing and oversight bodies.
	Ordinary financial support	High (100)	To support MFB's financial position and lending, Hungary has strengthened MFB's capital position on several occasions.
Likelihood of exceptional support	Strategic importance	High (100)	Unique policy role to support the country's key economic and public objectives; high-level cooperation with other national promotional institutions and the EU.
	Substitution difficulty	High (100)	MFB does not compete with other government-related financial institutions. The risk that MFB's business model would change is remote.
	Default implications	High (100)	A hypothetical default by MFB on its debt could lead to political and reputational repercussions. Additionally, there may be spill-over risks to other major GREs due to significant financial interdependencies with the Hungarian State and the domestic economy.
Final indicative notching			**0-1**

Appendix II. Selected financial information

	2018	2019	2020	2021	2022	2023
Balance sheet summary (HUF m)						
Assets						
Interest-bearing assets	881,935	1,119,324	1,568,065	1,812,930	1,975,700	2,280,665
thereof: Cash and debt securities	146,879	156,971	457,387	604,489	607,202	921,911
thereof: Loan portfolio	735,056	962,353	1,110,678	1,208,441	1,368,498	1,358,754
Non-interest-bearing assets	174,696	116,850	315,065	378,859	754,893	1,036,940
Other assets	172,465	191,260	185,601	209,880	239,384	223,732
Total assets	**1,228,603**	**1,427,433**	**2,068,731**	**2,401,669**	**2,969,978**	**3,541,338**
Total equity and liabilities						
Shareholders' equity	220,525	221,123	363,443	448,942	621,641	628,815
External funds	984,567	1,156,050	1,501,077	1,849,589	2,256,124	2,818,041
Other liabilities	19,372	46,355	202,339	99,663	87,507	88,236
Provisions	2,713	3,905	1,872	3,475	4,706	6,246
Total equity and liabilities	**1,228,603**	**1,427,433**	**2,068,731**	**2,401,669**	**2,969,978**	**3,541,338**
Income statement summary (HUF m)						
Total operating income	**13,201**	**11,267**	**15,903**	**28,188**	**54,178**	**48,440**
Net interest income	9,156	9,307	13,779	24,354	37,578	13,701
Dividend income	4,136	1,530	1,830	1,684	1,405	8,019
Net commission and fee income	-91	430	293	2,150	4,090	4,485
Total operating expenses	**-8,298**	**-11,707**	**-20,591**	**-20,179**	**-9,187**	**-10,262**
Expenses of banking operations	-9,833	-9,907	-10,893	-12,526	-13,728	-15,061
Personnel expenses	*-6,802*	*-6,837*	*-6,816*	*-7,752*	*-8,360*	*-9,096*
Other administrative expenses	*-2,732*	*-2,436*	*-3,071*	*-3,704*	*-4,050*	*-4,625*
Depreciation	*-299*	*-634*	*-1,006*	*-1,070*	*-1,318*	*-1,340*
Expense reimbursement	3,341	3,535	3,932	4,078	4,541	4,799
Effect on profit of changes in impairment and provisions	-1,806	-5,335	-13,629	-11,731	-26,722	-21,918
Other income/expenses	-883	840	-4,145	-3,624	-10,944	-13,946
Profit/loss for the year	**4,020**	**400**	**-8,832**	**4,385**	**6,194**	**2,345**
Selected ratios						
Return on assets (%)	0.3	0.0	-0.4	0.2	1.1	0.7
Return on equity (%)	1.8	0.2	-4.0	1.2	5.0	3.7
Cost-income ratio (%)	74.6	72.3	54.7	35.1	21.3	30.8
Leverage (total balance sheet/equity)	5.6	6.5	5.7	5.4	4.6	5.4
Liquid assets (% of total assets)	12.0	11.0	22.1	25.2	7.6	14.7
CET1 ratio (%)	26.7	20.9	22.4	16.6	16.6	16.2

Source: MFB, Scope Ratings

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Applied methodologies

Government Related Entities Rating Methodology, December 2024

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