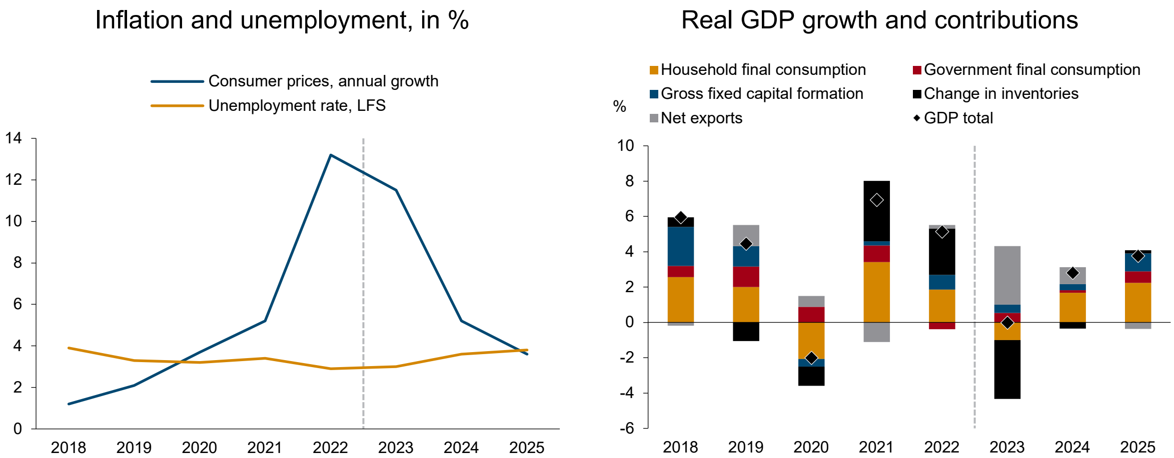
POLAND: Technically in recession

ADAM ŻURAWSKI

Restrictive monetary policy has pushed the economy into a minor recession that is directly linked to suppressed real wages and the liquidation of excessive inventories. The recent (6 September) cut in the policy interest rate is expected to prevent further deterioration on the real side. In effect, GDP in 2023 is likely to stay flat – and then to resume its moderate expansion in 2024. At the same time, disinflation will progress naturally. Public deficit spending remains high, but the public debt levels are not a serious threat to fiscal stability.

Figure 6.16 / Poland: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

GDP fell by 0.6% in Q2 2023 (year on year), following the 0.3% decline of Q1. This was due to a further fall in inventories, whose contribution to overall GDP growth reached -3.8 percentage points (pp). Household consumption fell by 2.7%, but public consumption rose by 2.6%. Gross fixed capital formation increased by 7.9%. With the volume of imports falling much more steeply than that of exports, the contribution made to GDP growth by foreign trade in goods and services turned markedly positive: 3.1pp (following a rise of 4.3pp in Q1 2023). Gross value added is continuing to contract in manufacturing, and particularly noticeably in the domestic retail trade and transportation/storage sectors.

The data available for Q3 2023 paint a rather unpromising picture. On the one hand, in July industrial production fell for the sixth consecutive month. Sales of manufactured durable consumer goods, intermediate goods and energy have continued to decline. However, sales of capital goods have kept on rising sharply (in July by over 10%, year on year). The growth in output of the export-oriented branches of industry is now slowing down, and the production of those industrial branches that supply mainly the domestic market has tended to stagnate or decline. To cap everything, retail sales have continued to perform quite badly. Finally, the business climate indicators in August were negative, with entrepreneurs remaining pessimistic, and the consumer confidence indicators similarly remained profoundly negative. The good news is that construction output rose by over 10% (January-July 2023) and the corporate sector's investment outlays have expanded quite considerably (over 10% in H1 2023).

There are signs of excess supply, reflecting inadequate demand. Firms supplying consumer durables and intermediate goods report the highest levels of excess supply. The excess supply conditions are reflected in inventories, whose levels are now considered by a large proportion of businesses to be too high. Excessive inventories of finished goods, now being scaled down, are adversely affecting the prospects for growth in production. Also, firms are finding it more difficult to pass their costs on to buyers in the shape of higher prices. Slight deflationary tendencies are already being captured by the statistics: the growth in producer price indices (PPIs) for industry and construction has been slowing, and in a number of manufacturing branches the price of articles sold has been declining. (In July and August, the PPI for manufacturing actually declined, year on year.)

The profitability of the entire corporate non-financial sector remains quite high, despite some recent deterioration. After a few quarters of corporate revenues rising much faster than their costs, the situation has reversed. Firms are now being induced to cut their markups somewhat. In effect, the net turnover profitability of the whole corporate sector declined to 5.1% in H1 2023 (from 6.1% the year before).

The labour market is in pretty good shape, though this is unlikely to last. The unemployment rate is low: 2.6% according to the Eurostat methodology (Labour Force Survey) and 5% by registration. However, the demand for labour has stopped rising, and business surveys suggest some decline in employment over the coming months. This is consistent with signs of weakening demand and sales.

Foreign workers remain important. Over 700,000 Ukrainians (predominantly female) have been registered as regular employees. In total, over 1m working foreigners currently contribute to the social security system. The unregistered employment of Ukrainians (as well as of other foreigners) is bound to be quite high, too. Quite likely their presence is reducing the bargaining power of regular employees and keeping a lid on wage hikes.

Wages have trailed slightly behind inflation, implying a gentle erosion of the real income of wage-earning households. On the other hand, the income of retired people has risen very sharply: in effect, the real monthly gross retirement pension has risen by over 6% year on year, and over 12% in the case of retired farmers. No doubt the generosity of the public pension system has much to do with the upcoming parliamentary elections (due 15 October).

Massive social transfers in the form of higher pensions and other extraordinary subsidies are helping to support private consumption and GDP growth (as well as to fuel inflation, at least partly). On the other hand, these transfers are increasing the size of the public-sector fiscal deficit (expected to reach about 5% of GDP) and the level of public debt. At about 50% of GDP, the latter is not going to be a serious menace to fiscal stability in 2023, though.

High inflation is still perceived to be a problem, although it has been declining consistently since February. In August, the consumer price index (CPI) stood at 10.1%. Part of that reflects the effects of hikes in administered prices. The CPI level has been constant for four consecutive months now. As it is becoming clear that the present inflation cannot be blamed on excessive consumer demand, price-wage spirals or some ill-defined ‘inflationary expectations’, there is fairly little that conventional restrictive monetary and fiscal policies can achieve. Further disinflation will follow naturally, as the price and cost effects of the initial negative shocks to the prices of imported energy carriers gradually fizzle out.

Monetary policy has been eased. Up until September, the key policy interest rate had been maintained at 6.75% (since September 2022). In the meantime, falling inflation had in effect tightened monetary policy, as in real terms the interest rate kept increasing. Since the recessionary effects of the monetary policy had become obvious, the central bank decided to cut its rates by 75 basis points (September 2023). Further, perhaps more moderate, cuts may follow in the coming months. This may be expected to affect the prevailing high (nominal) interest rates charged by the commercial banks, and thus strengthen private demand for consumer and investment credit. Thus far, the volume of household debt owed to banks has been falling (and that held by non-financial corporations has been increasing very slowly), while the volume of household and corporate bank deposits has been rising. Lower interest rates are expected to prevent entrenchment of the recessionary tendencies.

The exchange rate has temporarily depreciated in response to the interest rate cuts. For much of 2022 and 2023, the PLN/euro exchange rate fluctuated – often quite unexpectedly – at around 4.64. Those fluctuations did not reflect any obvious interest-rate movements. More recently, though (since April 2023), the exchange rate strengthened for a couple of months to stand close to 4.4. That development was hard to square with the fact that in the meantime, the European Central Bank kept increasing its policy rates. The interest rate cut in September immediately provoked a sharp weakening of the złoty which has returned to the values consistent with the longer-term means. That may positively affect the foreign trade balance, but it could also slow disinflation.

The disagreements with the European Commission are not yet of vital concern. The conflicts over a number of constitutional issues, which are unlikely to be resolved before the parliamentary elections, have already cost the country a large amount of money in the form of withdrawn EU funds. But given the country’s strong forex reserves, the Polish government is not yet ready to follow the ‘diktat of Brussels’. Possible delays (assumed in our forecast for 2023) in the transfer of EU funds to Poland are not yet a particularly grave problem – at least not in the medium term. Things may not be that easy in 2024 and beyond.

The elections (due on 15 October) may not affect the economy (at least not in the medium term). The opposition parties appear unable to form a ‘united front’, so that the ruling coalition led by Mr Kaczyński’s Law and Justice (PiS) party may well stay in power. Despite high inflation, PiS enjoys popularity – especially among the less prosperous population strata that still relish the various social security transfers made over the past eight years. The last-minute ‘sweeties’ that the government is distributing quite lavishly are helping as well. It is fairly obvious that, if victorious, PiS will continue the economic policy pursued so far. A victorious opposition would have to follow this overall successful (at least so far) economic policy as well, at least for a year.

Table 6.16 / Poland: Selected economic indicators

	2020	2021	2022 1)	2022 January-June	2023 January-June	2023 Forecast	2024 Forecast	2025 Forecast
Population, th pers., average 2)	37,899	37,747	36,822	.	.	38,360	38,370	38,380
Gross domestic product, PLN bn, nom.	2,338	2,631	3,078	1,420	1,607	3,390	3,660	3,950
annual change in % (real)	-2.0	6.9	5.1	8.0	-0.8	0.0	2.8	3.8
GDP/capita (EUR at PPP)	22,860	25,070	28,040	.	.	.	.	.
Consumption of households, PLN bn, nom.	1,300	1,455	1,721	840	936	.	.	.
annual change in % (real)	-3.6	6.2	3.3	6.8	-2.8	-1.8	3.0	4.0
Gross fixed capital form., PLN bn, nom.	428	442	513	199	232	.	.	.
annual change in % (real)	-2.3	1.2	5.0	8.7	7.2	2.8	2.1	6.0
Gross industrial production (sales) 3)								
annual change in % (real)	-1.2	14.5	10.6	14.7	-2.1	-2.0	4.0	5.0
Gross agricultural production								
annual change in % (real)	8.0	-1.7	2.2	.	.	.	.	.
Construction industry 2)								
annual change in % (real)	-3.5	1.5	7.6	15.0	1.2	.	.	.
Employed persons, LFS, th, average 4)	16,441	16,656	16,742	16,742	16,851	16,780	16,680	16,630
annual change in %	-0.1	2.6	0.5	1.4	0.7	0.2	-0.6	-0.3
Unemployed persons, LFS, th, average 4)	537	580	498	495	474	520	620	660
Unemployment rate, LFS, in %, average 4)	3.2	3.4	2.9	2.9	2.8	3.0	3.6	3.8
Reg. unemployment rate, in %, eop	6.8	5.8	5.2	5.2	5.0	.	.	.
Average monthly gross wages, PLN 5)	5,226	5,683	6,346	6,422	7,234	7,120	7,750	8,270
annual change in % (real, gross)	2.9	3.3	-2.1	0.9	-1.8	0.6	3.5	3.0
Consumer prices (HICP), % p.a.	3.7	5.2	13.2	10.9	14.2	11.5	5.2	3.6
Producer prices in industry, % p.a.	-0.5	8.1	23.8	22.0	11.6	12.0	8.0	4.0
General governm. budget, EU def., % of GDP								
Revenues	41.3	42.3	39.8	.	.	40.3	40.1	40.5
Expenditures	48.2	44.1	43.5	.	.	45.1	45.5	44.0
Net lending (+) / net borrowing (-)	-6.9	-1.8	-3.7	.	.	-4.8	-4.0	-3.5
General gov. gross debt, EU def., % of GDP	57.2	53.6	49.1	.	.	48.2	51.0	52.5
Stock of loans of non-fin. private sector, % p.a.	0.4	4.6	0.2	5.7	-3.1	.	.	.
Non-performing loans (NPL), in %, eop	7.0	5.8	5.6	5.6	5.6	.	.	.
Central bank policy rate, % p.a., eop 6)	0.10	1.75	6.75	6.00	6.75	5.75	5.00	4.00
Current account, EUR m 7)	12,820	-8,268	-19,618	-10,724	9,915	8,500	4,400	6,000
Current account, % of GDP 7)	2.4	-1.4	-3.0	-3.5	2.9	1.2	0.6	0.7
Exports of goods, BOP, EUR m 7)	220,604	263,740	320,361	154,633	168,675	345,000	379,500	413,700
annual change in %	0.1	19.6	21.5	20.8	9.1	7.7	10.0	9.0
Imports of goods, BOP, EUR m 7)	213,625	271,363	344,614	166,569	162,816	350,800	378,900	420,600
annual change in %	-4.9	27.0	27.0	32.3	-2.3	1.8	8.0	11.0
Exports of services, BOP, EUR m 7)	58,308	68,731	91,154	42,490	47,396	99,800	105,300	114,800
annual change in %	-7.4	17.9	32.6	34.5	11.5	9.5	5.5	9.0
Imports of services, BOP, EUR m 7)	35,329	41,934	54,694	24,501	27,649	58,500	61,400	65,400
annual change in %	-9.1	18.7	30.4	34.5	12.9	7.0	5.0	6.5
FDI liabilities, EUR m 7)	16,646	31,371	33,085	19,509	8,913	24,000	.	.
FDI assets, EUR m 7)	4,132	7,964	6,974	3,151	1,766	6,000	.	.
Gross reserves of CB excl. gold, EUR m	114,299	134,654	143,949	134,943	151,155	.	.	.
Gross external debt, EUR m 7)	307,412	322,710	348,068	.	.	360,900	373,800	395,800
Gross external debt, % of GDP 7)	58.4	56.0	53.0	.	.	49.4	47.7	47.1
Average exchange rate PLN/EUR	4.4430	4.5652	4.6861	4.6329	4.6259	4.64	4.67	4.70

1) Preliminary. - 2) From 2022 according to census 2021. - 3) Enterprises with 10 and more employees. - 4) From 2021 the new LFS methodology is applied in line with the Integrated European Social Statistics Regulation (IESS). - 5) Excluding employees in national defence and public safety. - 6) Reference rate (7-day open market operation rate). - 7) Including SPE.

Source: wiiw Databases incorporating Eurostat and national statistics. Forecasts by wiiw.