Polish
Economic
Institute

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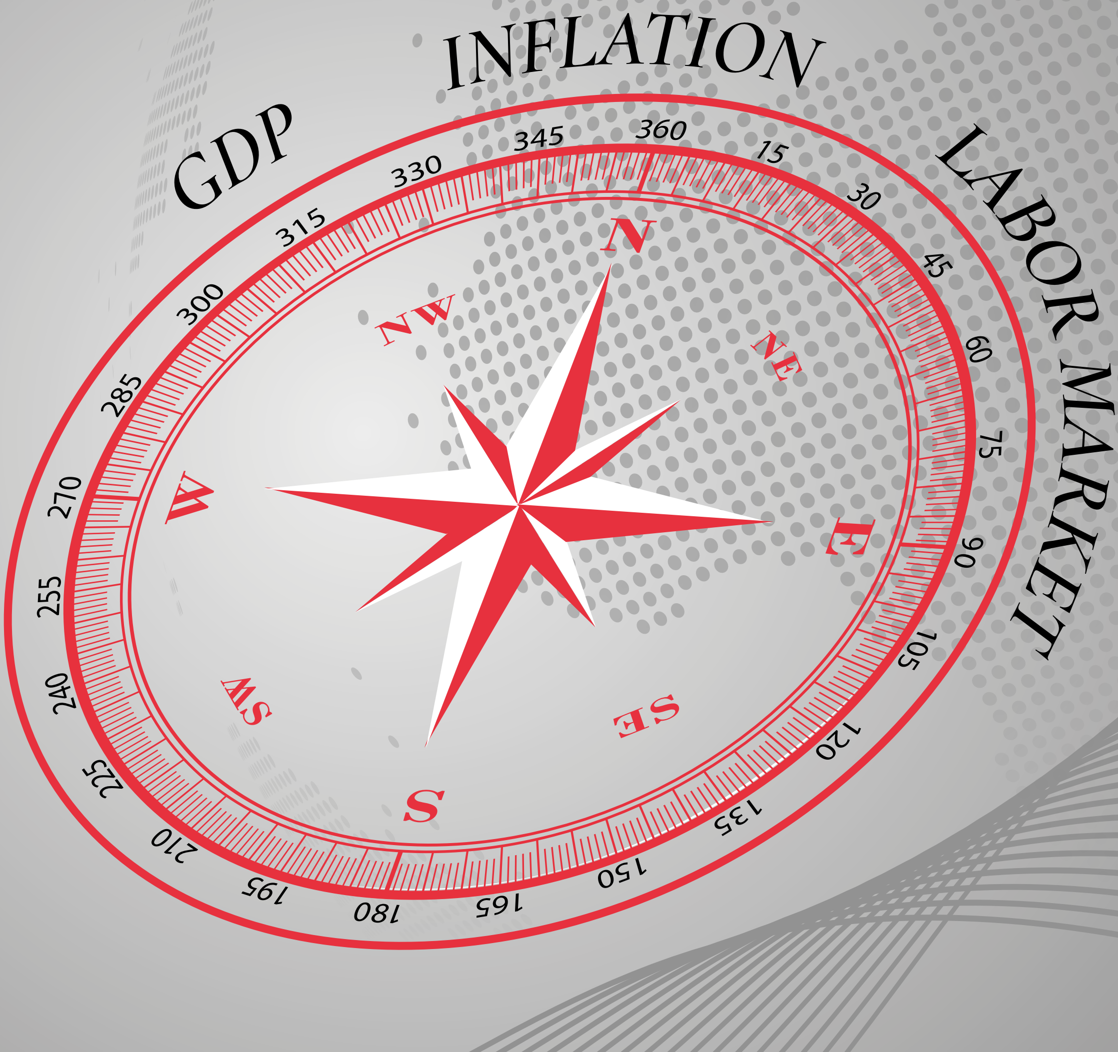

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Key numbers

0.8%
GDP growth in 2023

2.2%
GDP growth in 2024

12.6%
average CPI inflation in 2023

7.7%
average CPI inflation in 2024

6.2%
unemployment rate at the end of 2023

5.7%
unemployment rate at the end of 2024

11.3%
average wage growth in 2023

9.3%
average wage growth in 2024

Key findings

Over the next two years, economic growth will be relatively low. We expect the Polish economy to grow by just 0.8% in 2023 and 2.2% in 2024. Economic growth is mainly being driven by public spending and corporate investment. At the same time, household consumption will grow slowly. GDP growth this year will also be lowered by the fall in inventories.

We are revising our GDP forecasts downwards. Total growth over the next two years will be 1.3 pp lower than we forecast in December. The weaker forecasts are linked to the poor economic situation in the eurozone and potential threats to the stability of the financial sector in Europe and the US.

Despite the slowdown, the period of higher inflation will be longer than we anticipated in December. The average price increase in 2023 will amount to 12.6%, less than 0.5 pp lower than we estimated. However, only energy and fuel prices have slowed down more rapidly than expected. Core inflation is higher than we assumed. We therefore expect prices to increase by 7.7% in 2024 an upwards revision of more than 1 pp. We also anticipate worse conditions in 2025. There is a major risk linked to increase of energy prices.

The situation on the labor market is stable. We estimate that the unemployment rate will increase to 6.2% at the end of the year or in Q1 2024 – higher than we indicated in December. At the same time, wages are growing more rapidly than we forecast. In 2023 we expect an increase of 11.3%, 0.5 pp more than forecast in December.

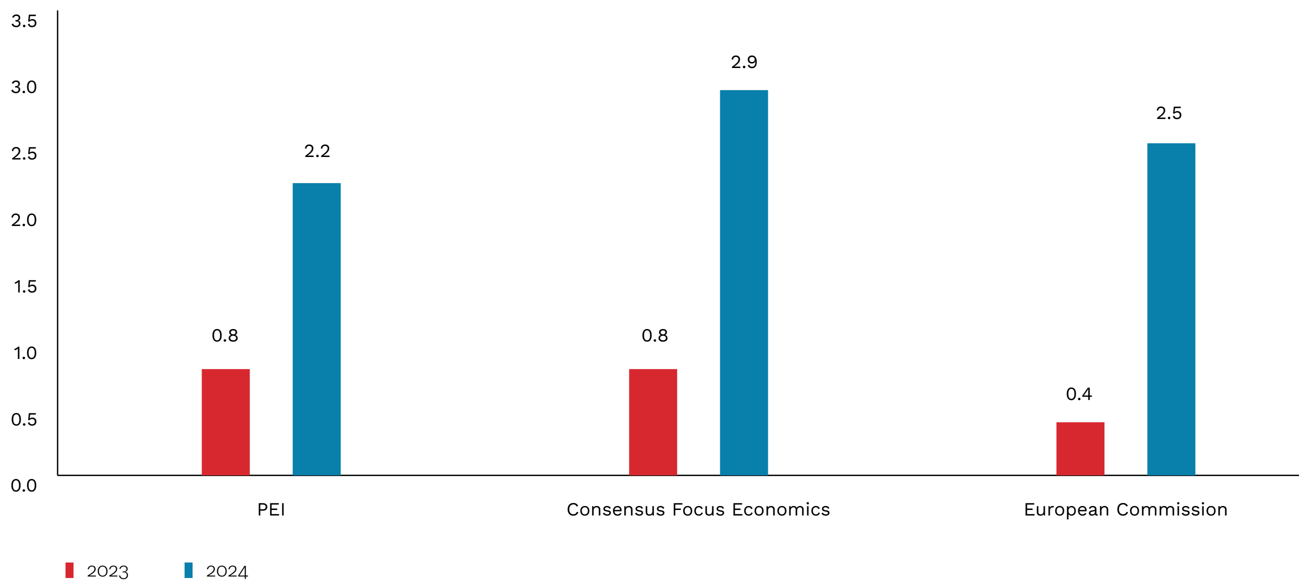
1. The Polish economy in Q1 2023

The Polish economy is just reaching the bottom of the slowdown. Data on retail sales and industrial production indicates clearly that the economy will be smaller than a year ago. However, this is largely the effect of the high point of reference: last year brought an unusually high increase in corporate inventories. The data in the coming months will probably be weak, too — when the war began, there was an influx of refugees, which increased spending on basic products and masked the weakening spending on durable goods in Poland. The number of Ukrainian migrants decreased in Q4 2022 which will be reflected in the decline in consumer spending in H1.

Inflation has peaked. In February, it amounted to 18.4%, but we will see declines linked to fuel and food prices in the months ahead. The cost of fuels and agricultural raw materials is currently lower than right after the war began, which is reflected in retail prices. However, the wide spread of inflation and increase in core inflation remain a problem. We estimate that the indicator reached 12.2% in March and that the coming months will only bring slight decreases.

High inflation is fuelling wage increase expectations. Wage growth at the start of the year is still double-digit, supported by the sharp increase in the minimum wage. In addition, in business climate surveys, a record percentage of enterprises indicated that they plan to increase wages in the near future. This is likely to perpetuate the high inflation.

Chart 1. Forecasts of Poland's GDP growth in the next 2 years



Source: prepared by PEI.

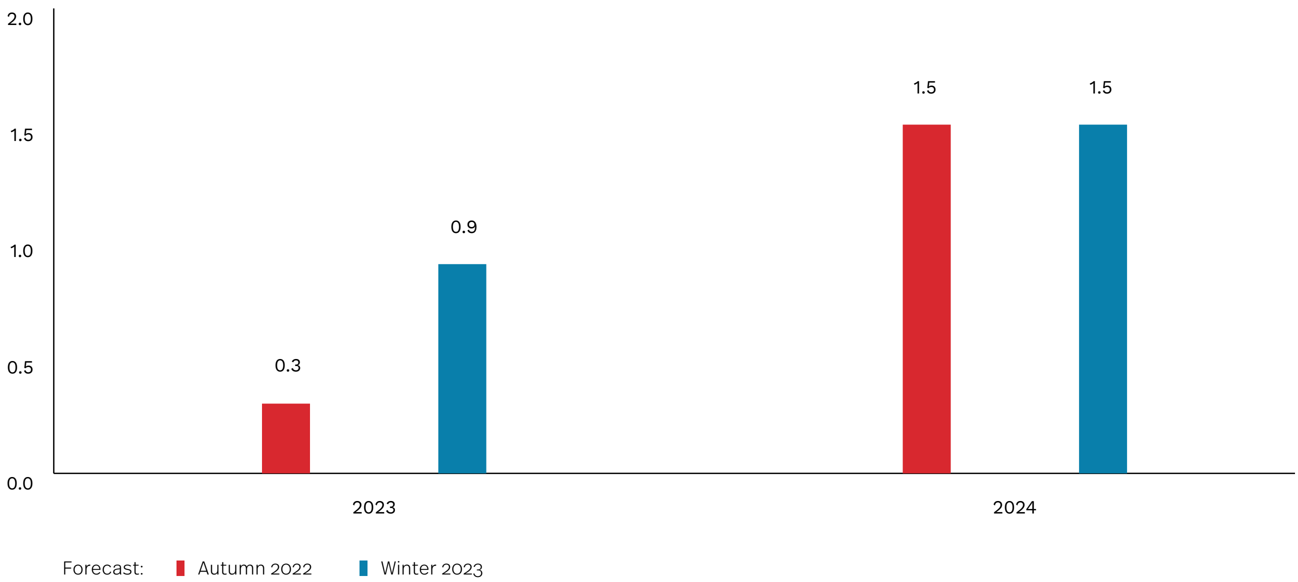
2. The global economy in 2023-2025

2.1. The European Union

In 2023 economic growth in the EU will be much weaker than in 2022. The European Commission (EC) forecasts that GDP growth will slow down from 3.5 to 0.9% y/y. In the eurozone, it will be a decrease from 3.5 to 0.8%. The German economy will perform the worst: analysts expect a poor result of 0.2%. In the eurozone countries, GDP growth will only exceed 1.5% in Slovakia and in three small economies (Malta, Luxembourg and Ireland).

The situation is better than forecasts in the autumn indicated. The EC's analysts have raised this year's GDP forecast for the eurozone by 0.6 pp, to 0.9%. This is the result of the warm winter and lack of problems with gas supplies. In addition, PMI surveys point to an improvement in the business climate in services; the index increased from 48.5 points in November to 55.6 points. in March. In industry, it remains at a level suggesting a contraction (48.5 points).

Chart 2. GDP growth forecasts in the eurozone (%, y/y)

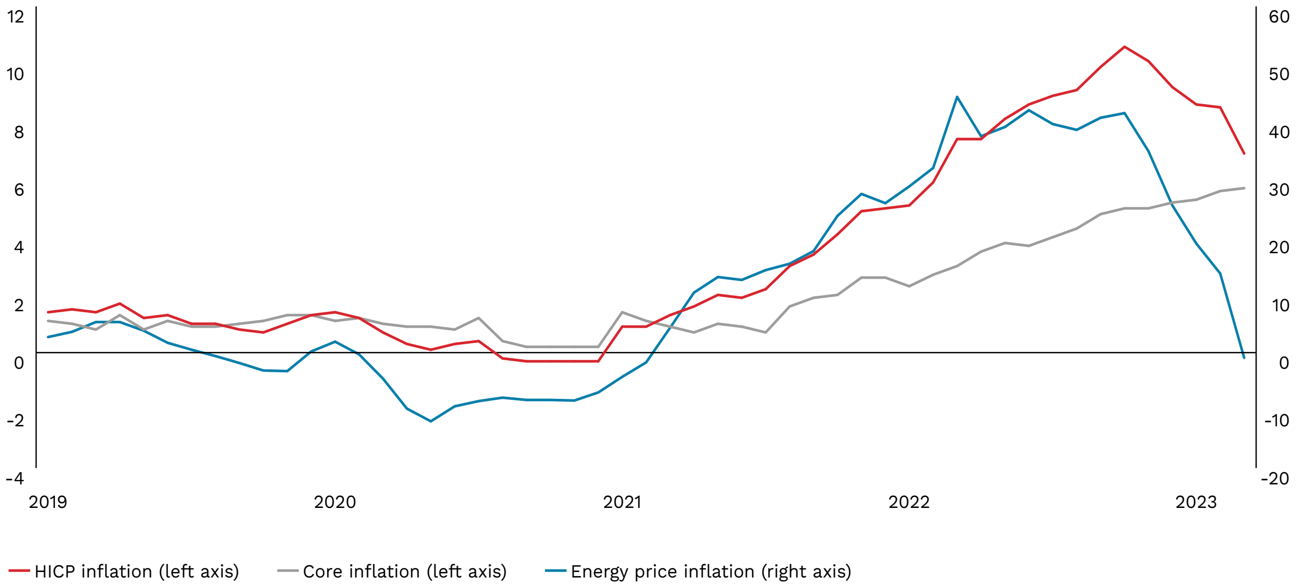


Source: prepared by PEI based on European Commission data.

However, high energy prices, which will hamper activity in industry, are still a threat. Energy commodity prices have fallen significantly compared to the first months after Russia invaded Ukraine; for example, Dutch TTF gas prices fell from EUR 110 to EUR 44/MWh over the course of the year. Nevertheless, they are still 2-3 times higher than before the pandemic and the chances of further decreases are small. These high prices are reducing European energy-intensive companies' competitiveness; for example, in February, German chemical company BASF announced its decision to reduce production. Analysts polled by Focus Economics predict that the collapse of energy-intensive industries will result in a decline in production in all major EU economies this year.

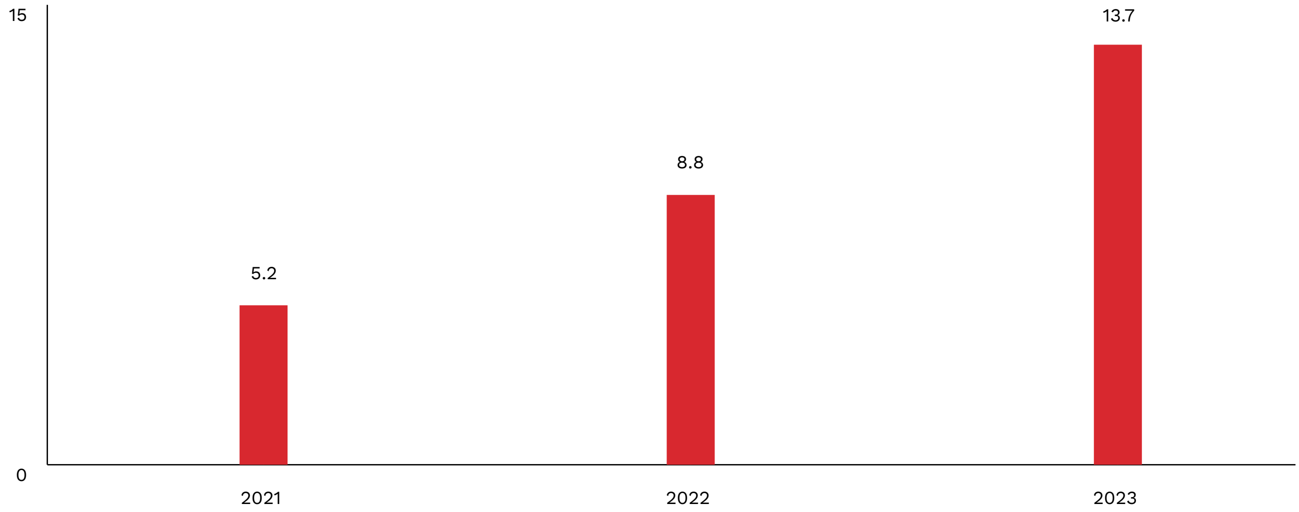
The eurozone also has a problem with high core inflation. HICP inflation in the eurozone fell from 10.6% y/y in November to 6.9% in March. This is mainly the effect of a lower increase in energy and fuel prices. However, core inflation continues to rise. In March, it amounted to 5.7%, a record high. The higher price growth in this category will be long-lasting; the macroeconomic forecast consensus indicates that inflation in 2023 will average 5.7% and still be above the ECB target (2%) in 2024.

Chart 3. Inflation in the eurozone remains high (%, y/y)



Source: prepared by PEI based on Eurostat data.

Chart 4. The German Vereinte Dienstleistungsgewerkschaft trade union's wage demands



Source: prepared by PEI based on Vereinte Dienstleistungsgewerkschaft's collective bargaining.

The high inflation has put a lot of pressure on salaries in Western Europe. In 2021 the largest German trade union's wage demands averaged 5.2%. In 2022 this was 8.8%. In 2023 during the ongoing negotiations between the union and employers, it is 13.7%, on average. The demands are therefore comparable to the salary increases observed in Central Europe. The actual increases are below the original demands, but the difference is usually 1-2 pp.

2.2. The United States

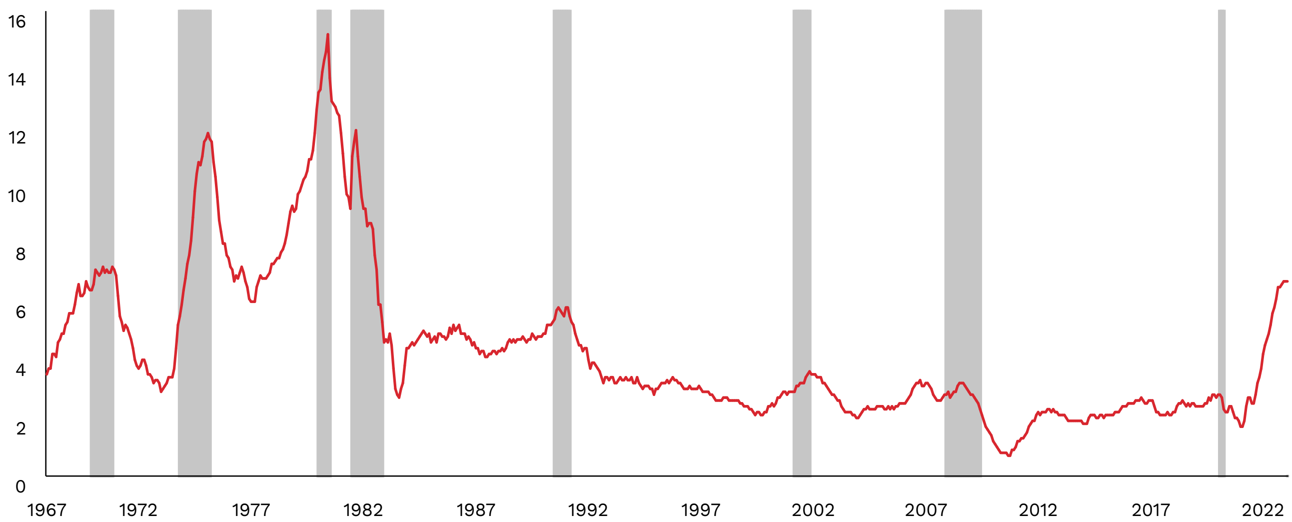
In the US, growth will be weaker in 2023 than in 2022 like in EU countries. The US monetary authorities expect GDP growth to slow down from 2.1% to 0.4%. The quarterly annualised growth rate[1] reported by the Bureau of Labor Statistics reached 3.2% in Q3 and 2.6% in Q4 2022. Forecast models suggest that good activity will be maintained in early 2023; at the time of writing, the GDPNow model estimate points to 2.5% growth in Q1.

The central bank's forecasts are clearly weaker than market estimates. After a strong first quarter, the Fed's forecasts will only be correct if the American economy finds itself in recession in the autumn. This scenario is currently being contested by commercial institutions: analysts surveyed by Focus Economics expect a growth of 0.9%.

The US continues to face high inflation. Consumer inflation in the US has been declining for three quarters; CPI fell from 8.9% in June 2022 to 6.0% in February 2023. The decrease is mainly the result of cheaper energy and slower growth in the prices of food and some durable goods. Market analysts forecast lower price growth in the coming months: according to the consensus, CPI will average 4.2%. Fed members are more optimistic - their forecast for the PCE price index is 3.3%.

Like in Europe, the problem is the persistence of inflation. The Fed's forecasts indicate that core inflation will reach 3.6%, higher than the main index. This is the result of a large increase in the prices of products and services whose prices are rarely changed. The Federal Reserve Bank of Atlanta measures these changes using sticky-price CPI. Since June 2022 this has increased from 5.4% to 6.6% y/y. This is the highest growth in this measure of inflation since the 1980s; historically, it has mainly declined in the aftermath of a recession.

Chart 5. Sticky core inflation in the US (%, y/y)

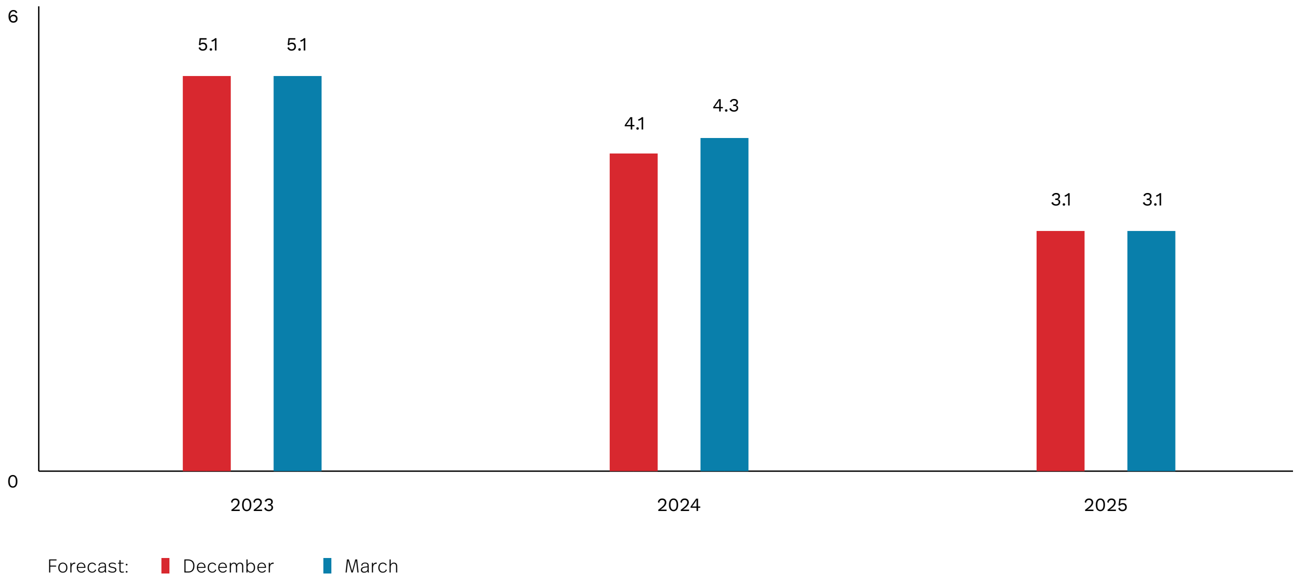


Note: The grey areas indicate periods when the US economy was in recession.
Source: prepared by PEI based on FRED data.

[1] Obtained by multiplying the quarterly growth rate by 4.

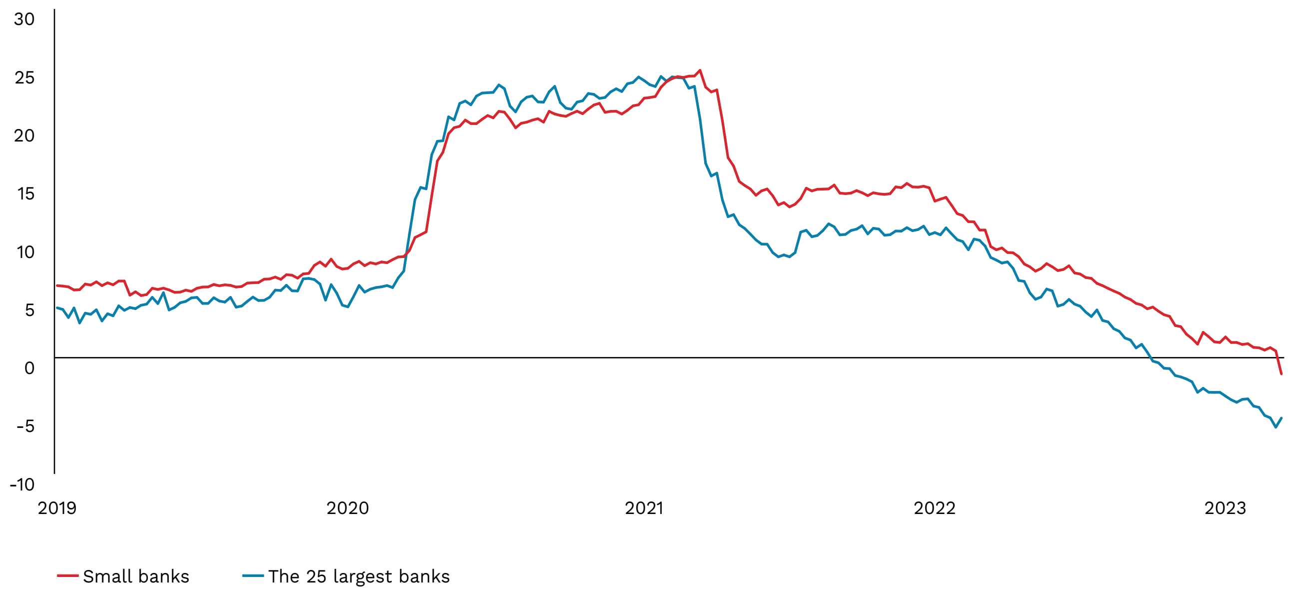
Despite the visible inflationary pressure, the Federal Reserve is slowly ending the rate-hike cycle. The Fed raised interest rates by 0.25 pp in March – the bank's main rate currently oscillates in the 4.75-5.0% range. Some analysts expect that this was the last decision of this kind this year; in our opinion, another rate hike in May is likely. The monetary authorities' decisions will depend on the situation on the labour market. Analysis by the Federal Reserve Bank of Atlanta indicates that the average wage in the US economy is growing by about 6%, and employment statistics remain at a record high. Nevertheless, the scale of the potential further rate hikes will be distinctly smaller than in previous quarters.

Chart 6. What will the Fed rate be at the end of the year



Source: prepared by PEI based on FOMC data, the Fed monetary authorities' expectations.

Chart 7. Deposits at American banks (% change, y/y)



Source: prepared by PEI based on FRED data.

The weakening of the rate hike cycle is linked to concerns about the outbreak of a financial crisis. In March, three US regional banks, Silicon Valley, Signature and Silvergate, collapsed. All three were linked to the financing of American start-ups or alternative investments in cryptocurrencies. Each collapse is a result of a mismatch between assets and deposits. These problems concern a specific segment of the US banking sector and are unlikely to translate into bankruptcies among larger banks. However, rising interest rates have two clear effects:

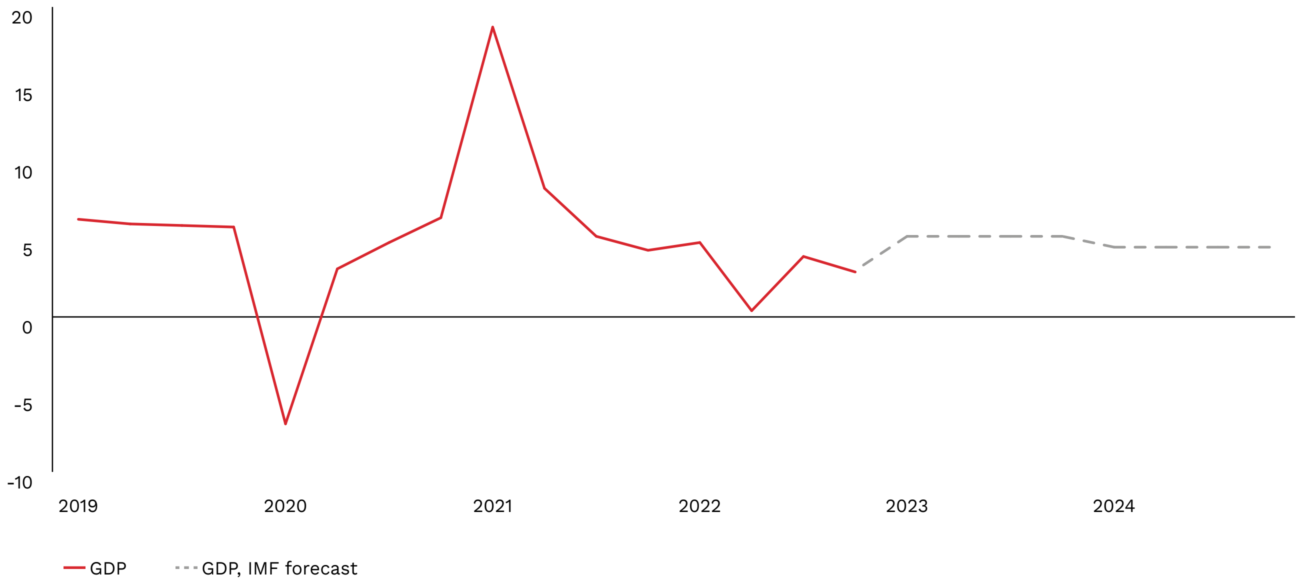
1) Some deposits are transferred from low-interest bank accounts to money market funds offering visibly higher interest rates. This effect primarily concerns the 25 largest banks in the US — the latest data shows that deposits there fell by 5.2% over the course of the year.
2) Higher financing costs will affect other sectors of the economy. Currently, tech companies and the real estate market, including that for commercial real estate, are the most sensitive to credit costs. These sectors have benefited from very preferential financing conditions in recent years. The main threat is the spread of the crisis from the office real estate sector. In subsequent quarters, the weakening economy will affect other industries, too.

2.3. China

After three years, China has abandoned its zero-COVID policy, which weakened the economy in 2022. GDP grew by just 3% then, the second-lowest result in the past 45 years, after 2020. In December, the Chinese government significantly eased the epidemic-related restrictions and, in January, announced the end of mandatory quarantine for visitors (OSW). Since then, sentiment in the economy has began to improve; PMI has risen to over 50 points in production and services.

Despite the change in attitude, China's economic growth in 2023 will be weak, too. The Chinese Communist Party has set a GDP growth target of 5% in 2023 below market forecasts (Bloomberg). This is much less than in previous years. Average growth over the past decade has been around 7%. The IMF also expects a slowdown: it forecasts GDP growth of 5.2% in 2023 and 4.5% in 2024. It will mainly be driven by private consumption; unlike in previous years, the forecasts assume a low share of investment.

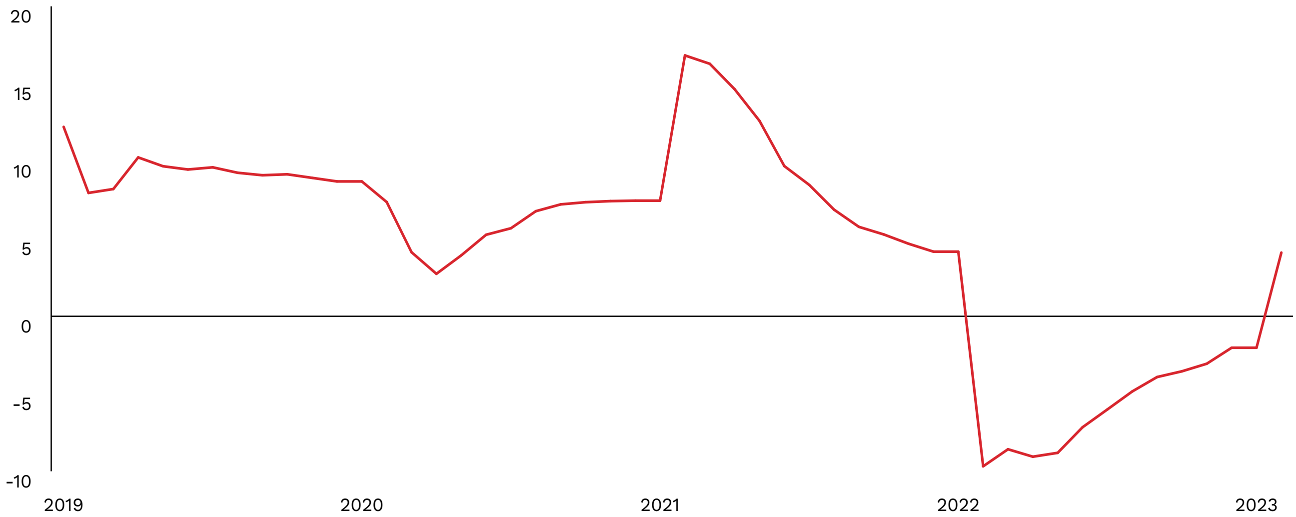
Chart 8. GDP growth in China (%, y/y)



Source: prepared by PEI based on IMF WEO.

The Chinese economy continues to face problems in the real estate market and demographics. The IMF indicates that the real estate crisis intensified in 2022. Housing prices have fallen to 2021 levels. In theory, the lifting of the restrictions allows for greater optimism — prices rose again at the beginning of the year. However, the large number of vacant buildings and ghost estates remains a problem. According to the Chinese statistical office, the area of unused space has increased by 100 million square metres over the past year; this is mainly residential space. The total area is 655 million square metres, close to the figure at the peak of the 2016-2017 crisis.

Chart 9. Increase in house prices in China (%, y/y)



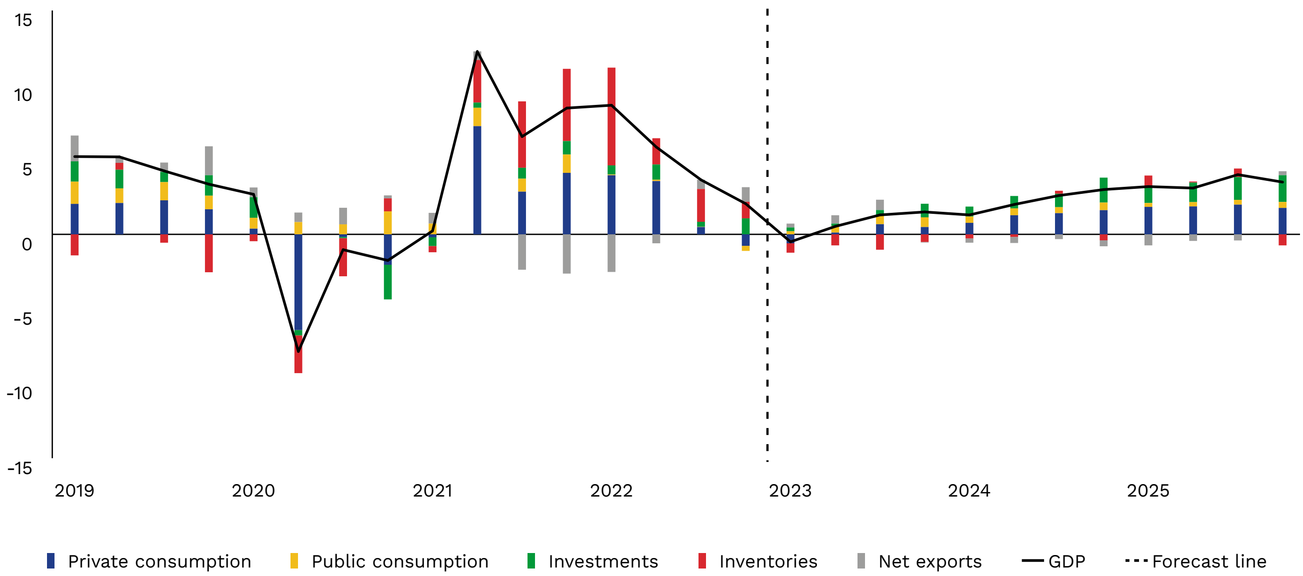
Source: prepared by PEI based on NBS data.

3. The Polish economy in 2023–2025

3.1. Economic activity – GDP

The Polish economy is facing a slowdown. In 2023 the rate of economic growth will fall to 0.8%, from 4.9% in 2022. The weakest results were probably recorded in Q1. when the economy contracted by around 0.5%. The following months will bring a slow recovery, with growth of 0.5 and 1.0%, respectively, mainly due to public spending and corporate investment. The results in 2024 will probably remain below Poland's economic potential; we forecast growth of around 2%.

Chart 10. Structure of GDP growth – PEI forecast (%, y/y)

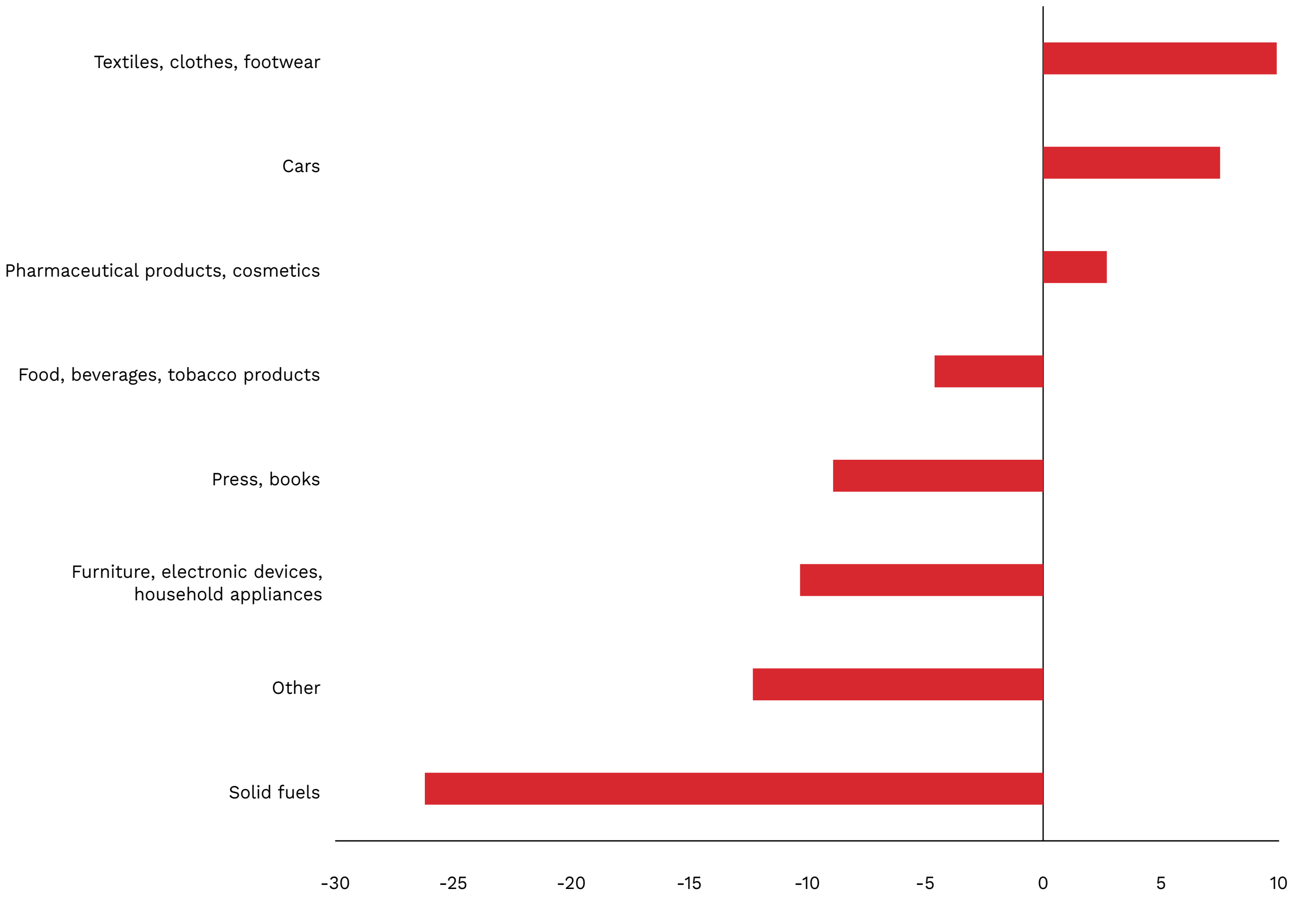


Source: prepared by PEI.

The weak economic growth is linked to the low growth in household consumption. In total, household spending will increase by a measly 0.2% in 2023. In Q4. consumer spending was 1.5% lower than the previous year. We expect a similar result in Q1 and low growth in Q2. A rebound will not take place until H2. The interest rate hikes and high inflation have lowered consumers' purchasing power. Since mid-2022 salaries have been rising more slowly than inflation, which decreases people's willingness to make larger purchases.

The poor consumption result is also the result of migrants' and refugees' departure from Poland. Retail sales fell by 5% in February. Food sales, among other things, were lower than a year earlier, while a slight increase was recorded in sales of cosmetics. This is the result of changes in migration: at the end of 2022 we observed an outflow of Ukrainians from Poland. In the coming months, migration will weaken consumer spending. The results between March and July 2022 were significantly boosted by spending by refugees from Ukraine and exceptional purchases to support migrants. We estimate that this increased GDP growth by 1 pp in 2022 but it will now contribute to the lower growth rate.

Chart 11. The sale of necessities fuelled the increase in consumption (%, y/y)



Source: prepared by PEI based on Statistics Poland data.

Economic growth will be based on investments to a greater extent. We expect the investment growth rate to fall from 4.5 to 2.6% in 2023 but it will still be more than three times higher than GDP growth. In H1. we expect moderate results: the freezing of mortgages sales will result in weak outlays on the housing market. During this period, greater changes will be linked to enterprises' spending on equipment and means of transport. In middle-2023 the implementation of pre-financed investments in infrastructure, industry and energy as part of Poland's National Recovery Plan (around 0.6% of GDP) will begin.

We expect a solid inflow of foreign investments. A survey conducted by logistics company Maersk shows that Poland is seen as one of the best countries to transfer production to; for example, from China (so-called nearshoring). Large investments have also been announced by automotive and machinery companies, including production lines linked to electromobility and heat pumps. The record spending relating to defence will be an additional stimulus.

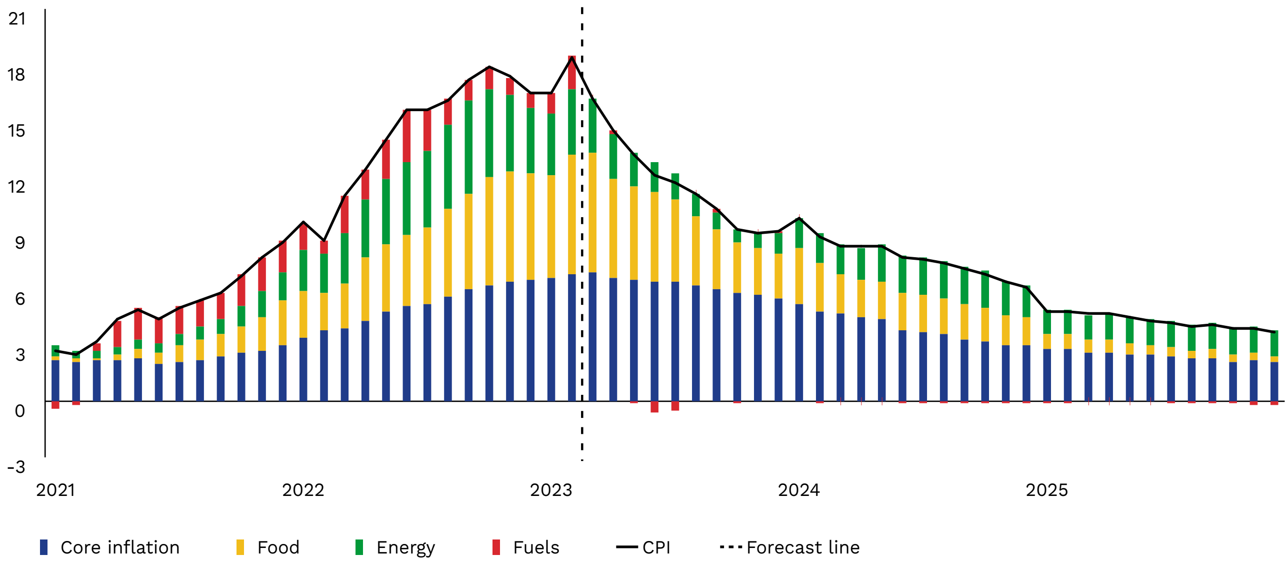
This year, net exports will increase Polish GDP. We estimate that foreign demand will boost the total growth rate by 0.3-0.4 pp. In Q1. Poland recorded a trade surplus. The improvement was supported by the sell-off of raw materials on global markets and the decline in imports of consumer goods. Weaker import growth is likely to continue for the first three quarters of the year.

Exports will continue to grow, despite the decline in industrial activity. We expect an average growth rate of 1.6%, around 0.6 pp higher than imports. Business climate surveys indicate that companies are seeing an increase in new orders. Assessments of enterprises' current and future situation are systematically improving. Since September, PMI has increased from 40.9 to 48.3 points.

3.2. Inflation

Inflation will remain high throughout 2023 and will not approach the target in 2024 either. We expect CPI to average 12.6% in 2023 and oscillate around 9% at the end of the year. Inflation has already peaked: it reached 18.4% in February and is currently declining. The main problem is still the stubbornly high core inflation: it is currently 12.2% and will only fall slightly in the coming months. Inflation will therefore remain high in 2024; 7.7% on average.

Chart 12. Structure of CPI inflation – PEI forecast



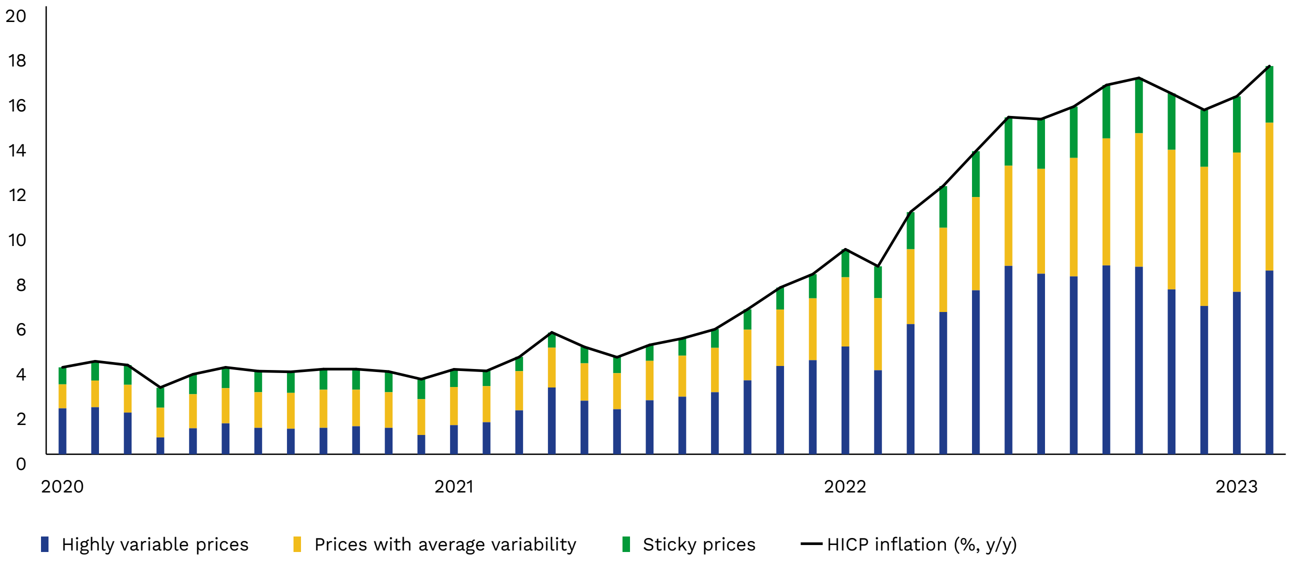
Source: prepared by PEI.

We are revising our core inflation forecasts upwards again. We expect that the price increase in this group in 2023 will average 11.1%, almost 2 pp more than we estimated in December. At the end of the year, it will be close to 10%. The high results are linked to the wide spread of inflation. Eurostat data shows that the percentage of consumer spending on goods and services in which prices are increasing by more than 5% is currently 93%. In addition, 70% of prices are increasing at a rate of over 10%.

Core inflation will decelerate gradually in 2023. We have broken down the structure of inflation based on the frequency of price changes, distinguishing between products with frequently-updated prices and those that are only updated very rarely. We estimate that products and services with infrequent price changes are increasing inflation by about 2.5 pp, and its core part by around 4 pp. This is five times more than in standard conditions. We expect only slight changes in the coming months; the slowdown in inflation in this group will be long-term due to the need to update prices in subsequent years with last year's inflation.

Core inflation will decrease in 2024. We expect that average price growth in this group will amount to 7%. The slowdown will be linked to the worse global economic situation and the interest rate hikes. The lower cost pressure already visible in the PPI indicator will help, too. Compared to previous quarters, enterprises' inflation expectations have also fallen.

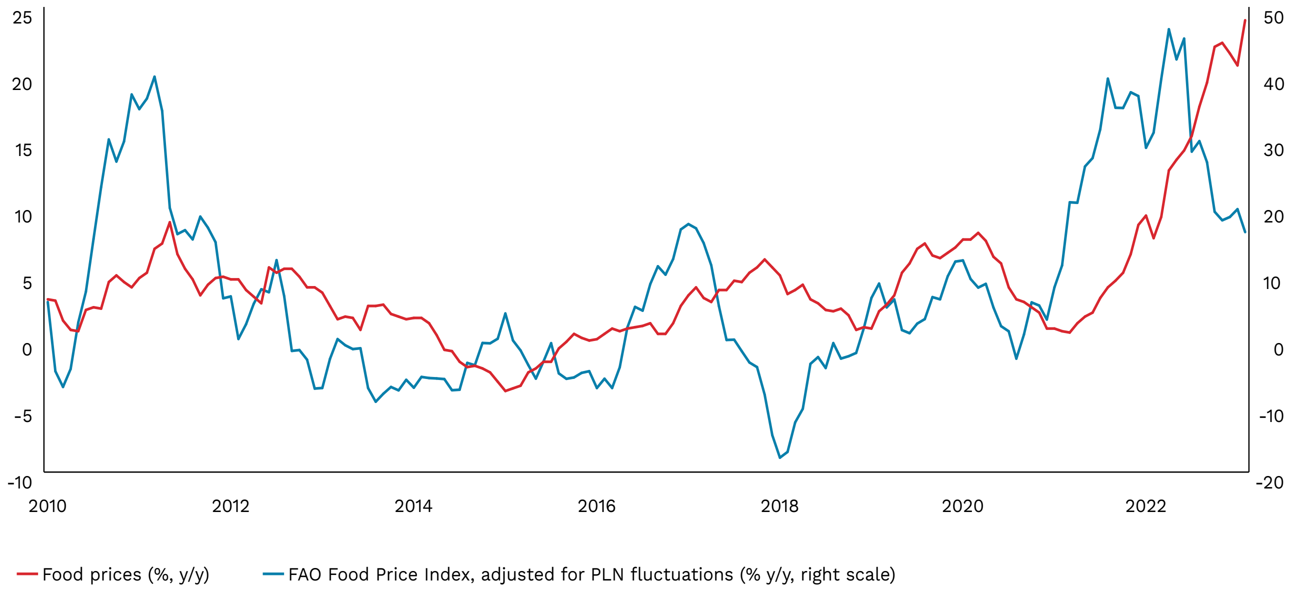
Chart 13. HICP inflation according to frequency of price changes (%)



Source: prepared by PEI based on Eurostat data.

Growth in food prices will play a much smaller role in the coming years. While it exceeded 20% in the last quarters of 2022 there will be a clear slowdown in the coming months. In total, at the end of the year, the growth rate should decrease to around 7%. The increase in global food prices has been slowing down for around five months and analysts surveyed by Focus Economics indicate that this trend will continue in the months ahead. However, a sharper deceleration is unlikely; in this case, too, we will not see lower until 2024. The growth rate will oscillate around 3-4%, mainly as a result of the return to standard VAT rates.

Chart 14. Increase in global and Polish food prices (%, y/y)



Source: prepared by PEI based on FAO and Statistics Poland data.

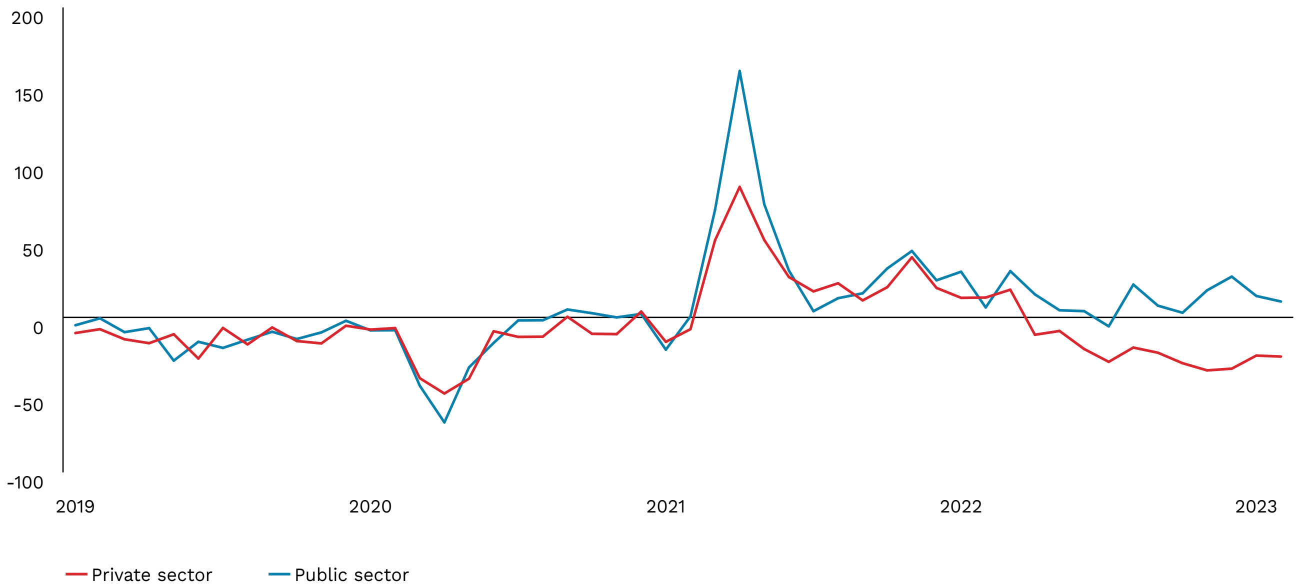
The increase in energy prices in 2023 will still be significant, but the peak is probably behind us. We expect that, in the coming months of 2023 it will slow down from 26.0% in February to around 12.3% at the end of the year. This will mainly be the result of lower coal prices for individual customers. Bills from professional heating plants will also grow more slowly. Electricity and gas prices will continue to increase throughout the year, following the return to standard VAT rates. Increases are possible at the end of the year as households exceed the limits up to which prices were frozen — much will depend on the measurement methodology used by Statistics Poland. The forecasts for 2024 are accompanied by high uncertainty; we expect energy prices to increase by around 16%, but much will depend on regulatory changes.

3.3. The labour market

Despite the economic slowdown, the labour market in Poland remains stable. Registered unemployment will remain in the 5.5-6% range for most of the year. The number of unemployed people registered in February was lower than a year earlier (by 6%). We expect unemployment to increase at the end of 2023 and at the beginning of next year, to around 6.2%.

The slowdown in the economy has mainly contributed to lower hiring. In February, companies advertised 25% fewer jobs than at the beginning of 2022. At the same time, a large percentage of companies still report labour shortages. Due to the economic slowdown in 2023 we expect a systematic slowdown in hiring, but the labour shortage will result in a small number of redundancies.

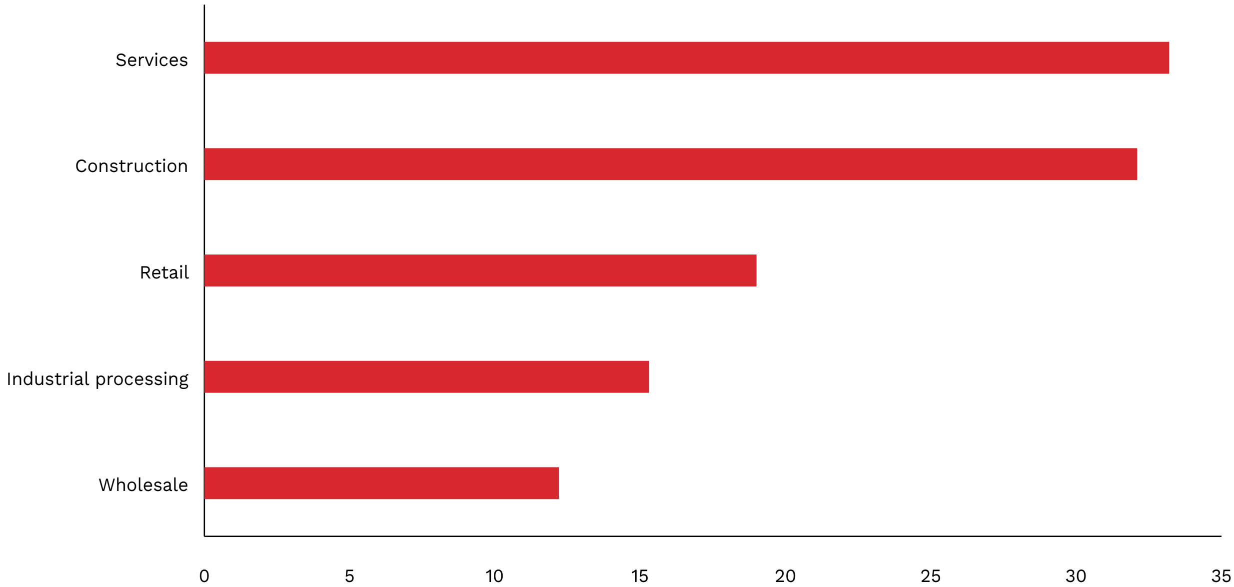
Chart 15. Growth dynamics of job offers in the private and public sector (%, y/y)



Source: prepared by PEI based on Statistics Poland data.

The number of collective layoffs remains low. According to Statistics Poland, 160 workplaces in Poland carried out collective layoffs in February, 36 fewer than a year ago. They concerned 14.627 people, a 30% decrease compared to last year. However, entrepreneurs' plans are more pessimistic. In March 2023 representatives of almost every industry declared that they would reduce employment over the next 12 months. The most pessimistic answers come from the construction industry, and the least pessimistic ones from transport and retail.

Chart 16. Shortage of workers in selected industries (% of enterprises that sees a shortage)



Source: prepared by PEI based on Statistics Poland data.

We expect unemployment to fall to around 5.7% in 2024. This year will be difficult for the labor market due to the high uncertainty. About 60% of companies cited it as the main barrier limiting their activity. However, activity should improve with the end of the year, in part due to public investments or improved sentiment among households.

In 2023 wage growth will remain in double digits. We expect the average wage to increase by 11.3%. The high inflation will contribute to the decrease in purchasing power in H1; the lower number of new job offers will make it more difficult for employees to negotiate wage increases. We expect the situation to improve in H2. when wages will grow 1% more rapidly than inflation. However, this will still be a weaker result than before the pandemic. Disposable income will grow more rapidly in 2024 — the wage growth rate will fall to 9.3%, but it will be higher relative to inflation.

Forecast table

Details	2023				2024			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Economic activity (%, y/y)								
GDP	-0.5	0.5	1.3	1.5	1.3	2.0	2.4	3.0
Household consumption	-1.0	0.2	1.2	1.0	1.3	2.2	2.5	3.3
Public consumption	1.2	2.3	3.2	3.1	2.3	2.4	2.1	2.4
Capital expenditures	2.0	1.0	2.2	4.2	5.2	5.3	5.5	7.5
Exports	0.3	0.7	2.5	2.9	3.4	3.3	4.0	4.5
Imports	-0.1	-0.2	1.4	3.0	3.3	3.6	4.2	5.0
Inflation (%, y/y)								
CPI	17.0	13.3	11.0	9.1	9.0	8.1	7.4	6.4
Core inflation	12.0	11.5	11.0	10.1	8.7	7.5	6.3	5.4
Labour market								
Registered unemployment rate	5.5	5.5	5.8	6.2	6.2	5.9	5.7	5.7
Wages in the national economy (%, y/y)	12.8	11.6	11.2	9.6	10.2	9.4	9.1	8.5

Details	2022	2023	2024	2025
Economic activity (%, y/y)				
GDP	4.9	0.8	2.2	3.5
Household consumption	3.0	0.4	2.3	3.4
Public consumption	-0.3	2.5	2.3	1.7
Capital expenditures	4.6	2.6	6.1	8.3
Exports	4.5	1.7	3.8	3.7
Imports	5.3	1.1	4.1	3.7
Inflation (%, y/y)				
CPI	14.3	12.6	7.7	4.3
Core inflation	9.1	11.1	7.0	4.3
Labour market				
Registered unemployment rate (end of year)	5.5	6.2	5.7	5.6
Wages in the national economy (%, y/y)	12.8	11.3	9.3	6.4

Source: prepared by PEI.

The basis for preparing the forecasts is the *Polish Economic Institute's macromodel of the national economy* (Welfe, 2020) developed in cooperation with external experts.

List of charts

The Polish Economic Institute

The Polish Economic Institute is a public economic think tank dating back to 1928. Its research primarily spans macroeconomics, energy and climate, foreign trade, economic foresight, the digital economy and behavioural economics. The Institute provides reports, analyses and recommendations for key areas of the economy and social life in Poland, taking into account the international situation.

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