



CEE Economic Monthly

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Content:

Macroeconomics:

Jakub Rybacki

@ jakub.rybacki@pie.net.pl

[@jakubrybacki2](#)

+48 512 275 365

Marcin Klucznik

@ marcin.klucznik@pie.net.pl

[@MarcinKlucznik](#)

+48 503 457 274

Sergiej Druchin

@ sergiej.druchyn@pie.net.pl

[@druchin_s](#)

+48 792 766 265

Sebastian Sajnog

@ sebastian.sajnog@pie.net.pl

[@BastianSajnog](#)

+48 501 837 748

Dawid Sułkowski

@ dawid.sulkowski@pie.net.pl

[@Dawid_Sulkowski](#)

+48 885 062 001

Energy:

Maciej Miniszewski

@ maciej.miniszewski@pie.net.pl

[@macminiszewski](#)

+48 799 126 992

► Industrial performance has declined noticeably across almost the entire EU, including Central and Eastern European (CEE). The slowdown is pronounced in energy-intensive sectors, where the declines are in double digits. Poland is proving to be resilient, compared to other countries. Looking ahead, we expect a rebound. We look at the outlook in the section: *The slowdown in energy-intensive industry in CEE*.

► Activity rates in energy production are correlated with manufacturing. Current EU policies incentive investments in efficiency. However, EU countries tend to struggle with achieving the ambitious targets set by the European Commission. More in the section: *Energy sector struggles with the transition*.

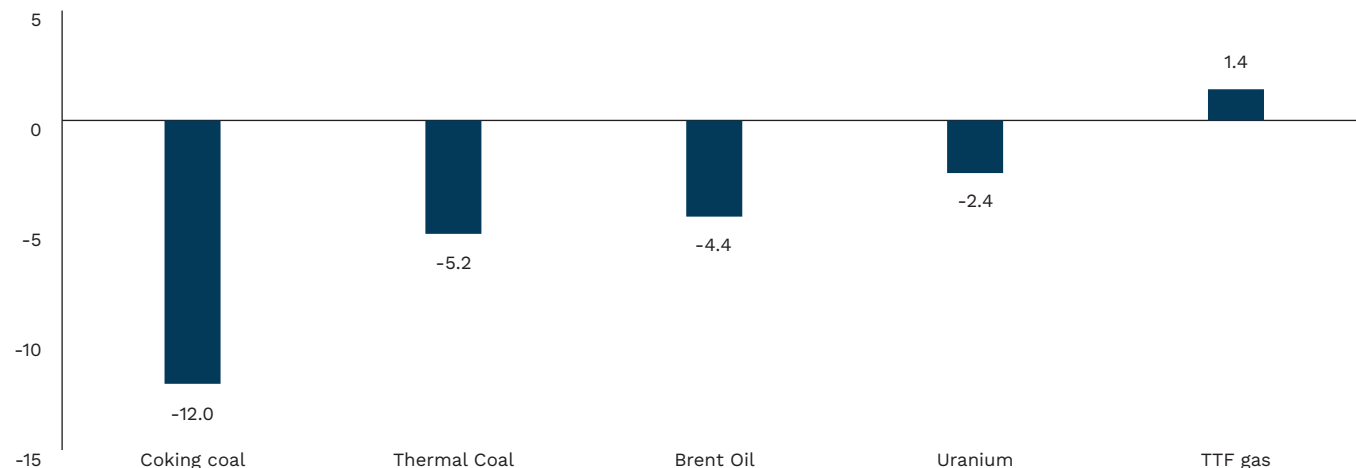
► MOL Hungary and Orlen Poland saw mixed financial results in 2023. Both benefited from strong oil and gas prices in 2022. However, they also face a number of challenges, including the need to transition to a low-carbon economy, and rising energy costs. We discuss the issue in the section: *Energy companies' profits normalised in 2023*.

► European governments tried to shield consumers and companies from unprecedented energy price increases. Consumer support is likely to be concluded soon; however, the energy prices are having a detrimental effect on competitiveness in industry. Germany has announced a new package to lower it. We examine whether CEE policies also support industry in the section: *National policies to shield companies in Germany and CEE*.

► Energy-intensive industry in Germany faces a challenge. Historically, expensive energy has not posed a significant problem. However, the energy crisis has widened the gap in competitiveness between Germany and economies outside Europe. This raise concerns about deindustrialisation, particularly within energy-intensive industries. More in the section: *Discussion: The impact of the energy shock on German Industry*.

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Expected change in energy commodity prices from Q4 2023 to Q4 2024 (%)



Source: Focus Economics.

The slowdown in energy-intensive industry in CEE

153.1%

level of production in Poland (Index, 2015=100)

-33.4%

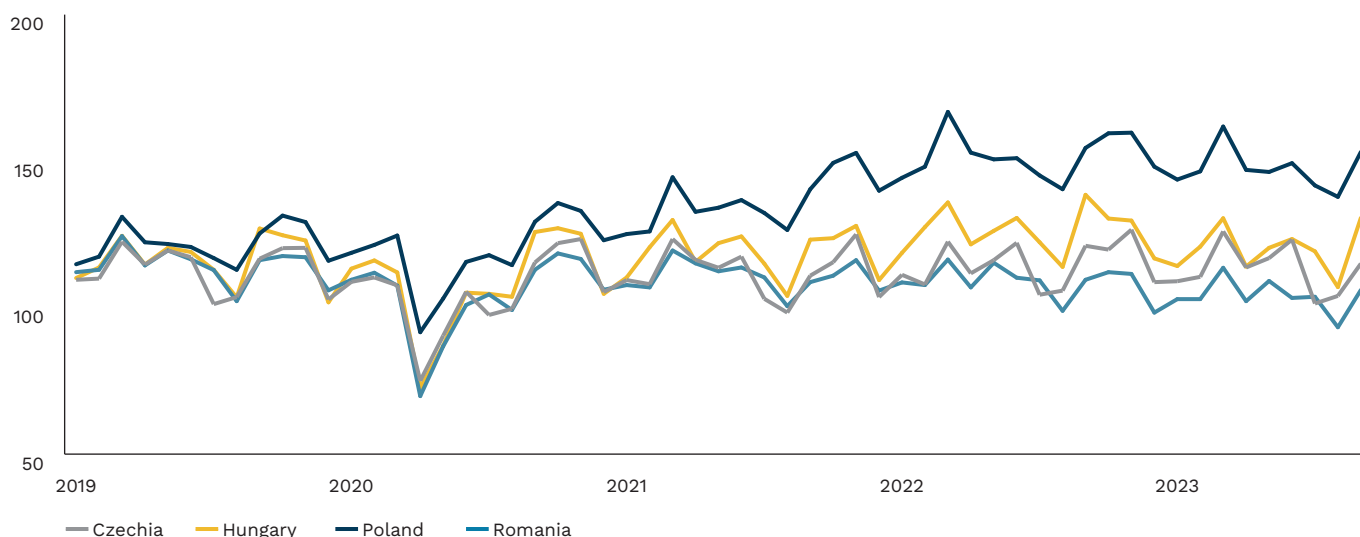
fall in metal production in Hungary in September, compared to January 2021

► Industrial performance has declined noticeably across almost the entire EU, including Central and Eastern European (CEE). The slowdown is pronounced in energy-intensive sectors, such as metal and chemical production, where the declines are in double digits. Poland is proving to be resilient compared to other countries. Looking ahead, we expect a rebound – the diminishing impact of energy shocks and a rebound in consumption are expected to reinvigorate industry, but growth should be slower than in recent years.

► **Weak industrial performance in Europe.** This year, there has been a discernible decline in industrial activity in Europe, echoing the broader weakening of the economy. Factors such as high inflation, lower consumer purchasing power, and more stringent monetary policies have contribute to this trend. According to Eurostat, industrial production in the EU dropped by 6.1% year on year in September. The magnitude of this decline varies between countries, with the CEE countries generally showing more resilience than other parts of the EU.

► **Polish industry stands out in CEE.** In September, Poland recorded a relatively modest decrease in industrial production of just 0.9%. In contrast, it fell by 5.0% in Czechia, by 3.2% in Romania, and by 5.7% in Hungary. This resilience is further underscored by the rapid expansion in Polish industry after the COVID-19 pandemic; industrial activity is now over 20% higher than in January 2020. In comparison, the recovery in other countries in the region has been less pronounced. The increase has been 8.7% in Hungary and 4.4% in Czechia, with a 5.0% decrease in Romania.

Figure 1.1. Industrial production in CEE (index, 2015=100)



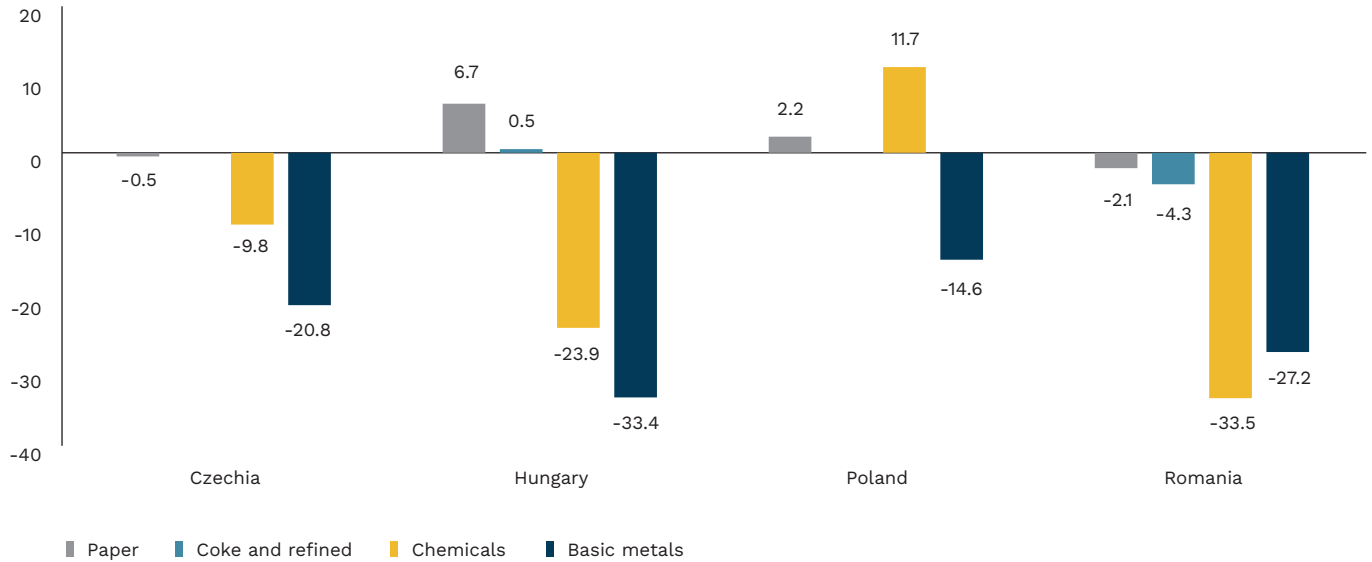
Note: seasonally and calendar adjusted data.

Source: Eurostat.

► **The slowdown in energy-intensive industries is significantly more pronounced.** This trend is largely a result of the ongoing energy crisis and the substantial rise in energy commodity prices, which peaked in mid-2022. Industries such as chemicals, metallurgy, glass, paper, coke, and petroleum product manufacturing, known for their high energy consumption during production, have been particularly affected. The escalating energy costs have had a negative impact on these

industries' operational efficiency, reducing production output. As a result, they have experienced a sharper decline in production, with a double-digit fall in activity in the chemical and metallurgical industries.

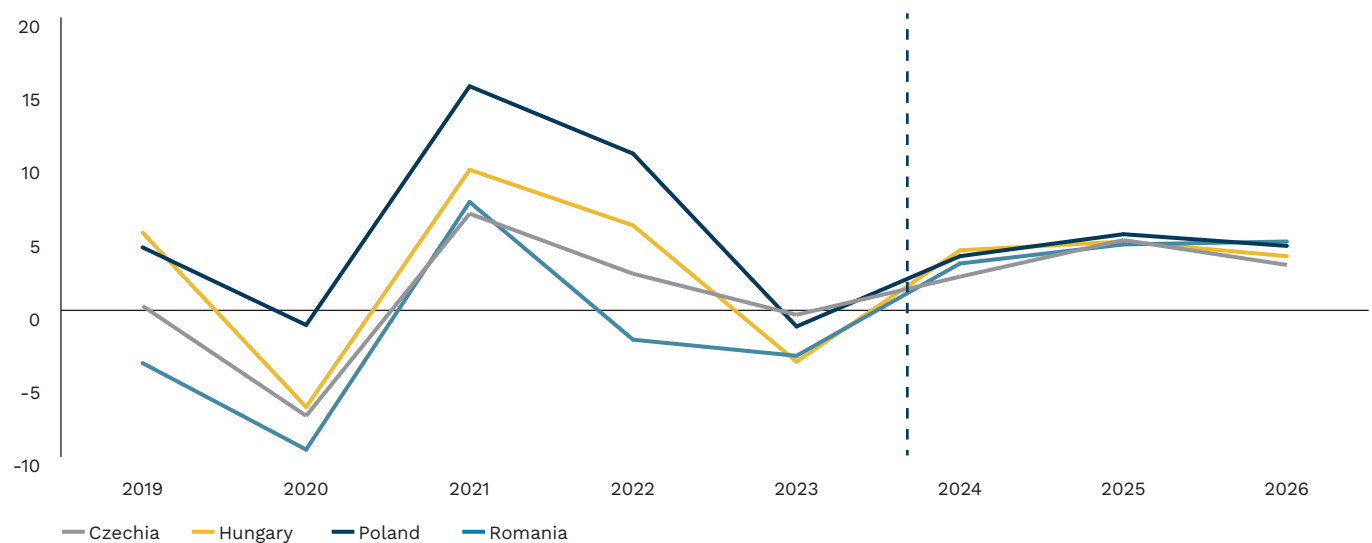
Figure 1.2. Decline in industrial production in energy-intensive sectors in CEE (compared to January 2021)



Note: seasonally and calendar adjusted data. No detailed data on coke and refined production for Czechia and Poland – the data is confidential.
Source: Eurostat.

► **The industrial landscape in CEE is expected to improve gradually.** According to the Consensus Forecasts by FocusEconomics respondents, a resurgence in industrial activity is expected to begin in 2024. This positive shift is primarily linked to the diminishing impact of the energy shocks that had hampered production, coupled with an increase in consumer purchasing power.

Figure 1.3. Annual production growth (% y/y)



Source: Consensus FocusEconomics.

Energy sector struggles with the transition

► Activity rates in industrial energy production are generally correlated with manufacturing. Manufacturing tends to grow slightly more rapidly, mainly due to technological change and investments in energy efficiency. Current EU policies incentivise a reduction in energy consumption. However, EU countries tend to struggle to achieve the ambitious targets set by the European Commission.

26%

industry's share in final energy consumption in the EU

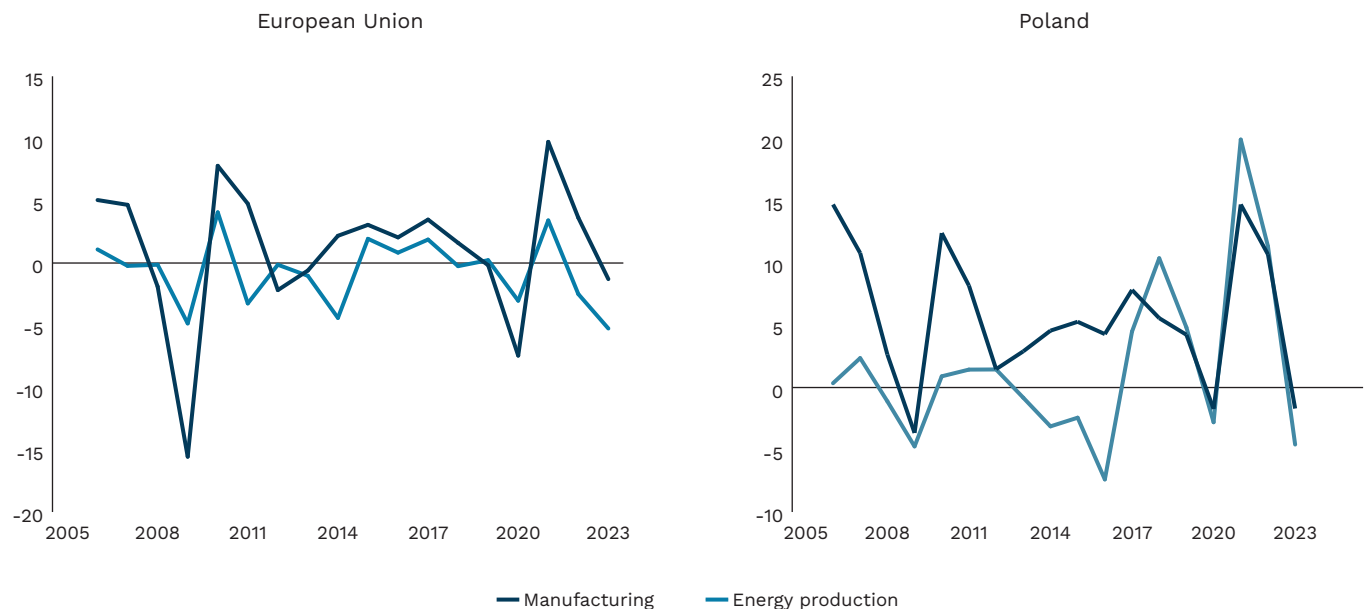
21.2%

required reduction in final energy consumption in the EU, compared to 2021

► **Activity in the energy sector is correlated with production in manufacturing.** As a rule, increases in activity in manufacturing are correlated with higher energy production. However, energy production in the last years was growing more slowly than manufacturing. There are a number of reasons for this:

- Part of the volume growth in manufacturing stems from improvements in technology and the production of higher value-added goods.
- Industry accounts for just 26% of the EU's final energy consumption, slightly less than households (28%) and transport (29%). Energy consumption in transport is mainly fuels, though.
- Part of the increase in electricity production from renewables comes directly from businesses and households; they are both producers and consumers. This reduces the production and supply of energy by industry counted in NACE section D.
- EU countries are investing heavily in greater energy efficiency; for example, reducing the amount of electricity needed in industrial processes, recycling heat, or cogenerating heat and electricity. These measures reduce overall energy demand without harming industrial activity.

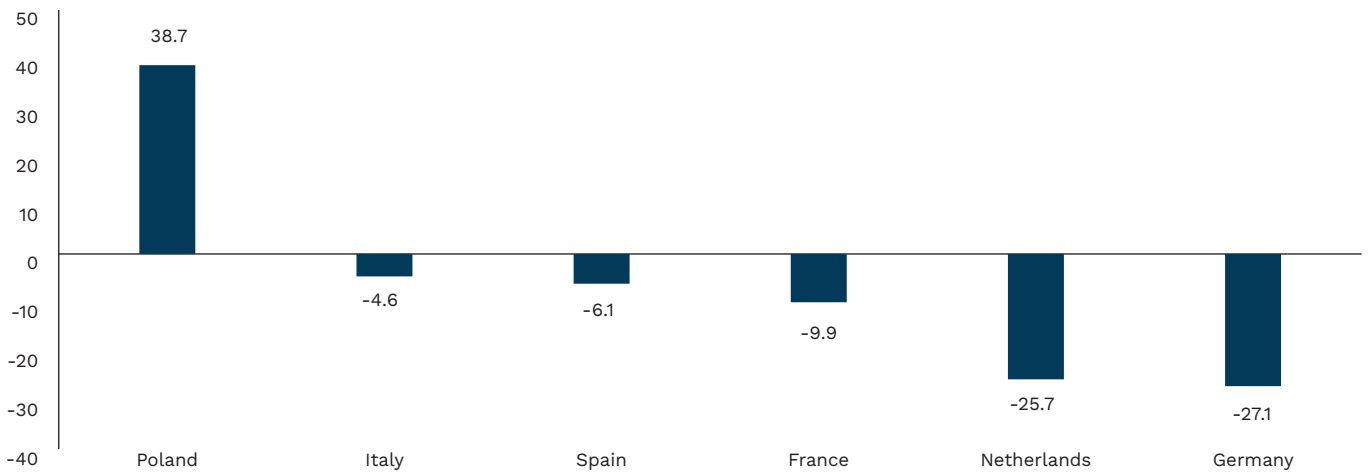
Figure 2.1. Energy and manufacturing production annual growth rates (%)



Source: Eurostat, NACE sections C and D, yearly averages of volumes, seasonally adjusted.

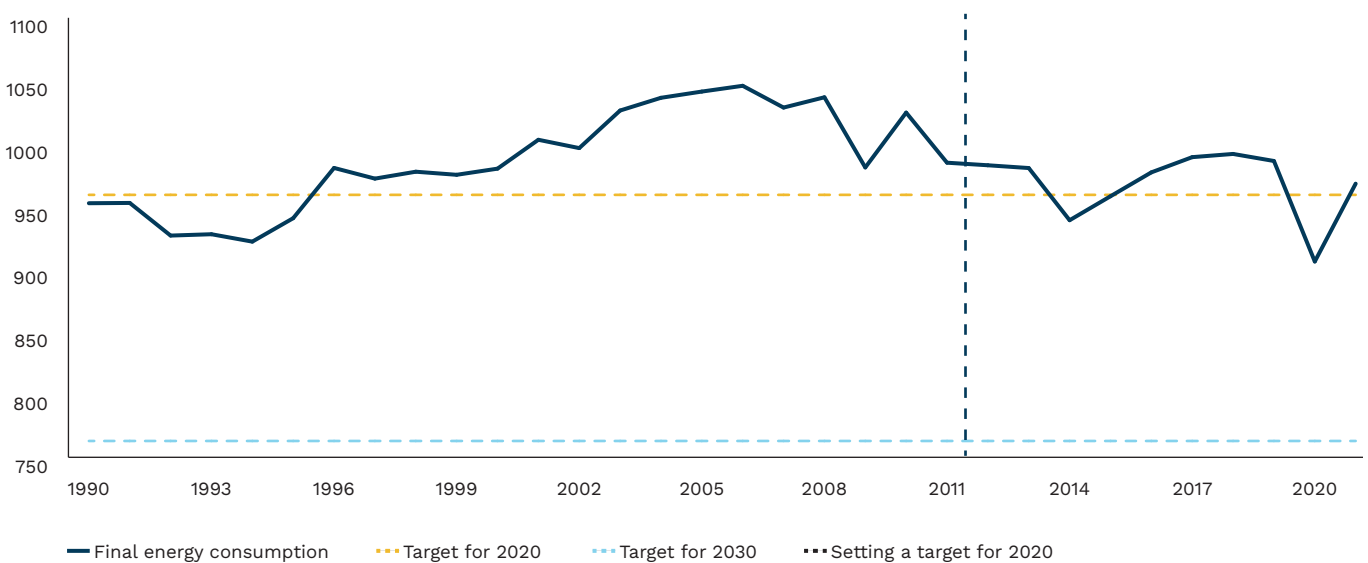
► **Energy production by industry in most EU economies is generally declining.** The total production volume in the EU-27 is now 5% lower than in 2015. There have been declines in virtually all the major EU economies, ranging from around 5% in Italy and Spain to over 25% in the Netherlands and Germany. The only exception is Poland, with total production growth has reached almost 40%, compared to 2015. **However, this indicator does not accurately reflect the state of the energy industry.** The large increase in industrial energy production in Poland partly results from the impressive growth in manufacturing. However, it is also partly due to the small share of renewable energy sources; in Poland, they account for 15.6% of final energy consumption, compared to an EU average of 21.8%. In addition, Polish companies have so far invested less in energy efficiency than their western counterparts.

Figure 2.2. Industrial energy production growth in the EU's six largest economies (% total increase in 2015-2023)



Source: Eurostat, NACE section D, yearly average of volumes, seasonally adjusted.

Figure 2.3. Final energy consumption in the EU (Mtoe)



Source: Eurostat.

► **The EU plans to increase energy efficiency.** The legal framework for these policies are the Energy Efficiency Directives. The first, adopted in 2012, aimed to reduce final energy consumption from 983 million tonnes of oil equivalent (Mtoe) in 2012 to 959 Mtoe in 2020, a 2.4% decrease. However, this target was not actually met. Formally, final energy consumption in 2020 was 905.9 Mtoe, lower than required by the directive, but this was merely the result of the COVID-19 recession. Final energy consumption in both 2019 and 2021 was above the Commission's target (by 2.8% and 0.9%, respectively).

► **In June 2023, the Commission revised its 2030 targets.** They had initially called for final energy consumption to be reduced to 846 Mtoe; the revised targets require it to fall to 763 Mtoe. This scenario would require a 21.2% reduction in consumption compared to 2021. Meeting this target would therefore require an annual reduction in final energy consumption of 2.6%. Some acceleration is likely given the increase in energy transition investments. However, achieving such an ambitious target – 10 times stricter than the previous one – seems difficult without negative pressure on industry and consumption.

Energy companies' profits normalised in 2023

15%

total drop in gas consumption in Hungary in 2022

17%

total drop in gas consumption in Poland in 2022

► MOL Hungary and Orlen Poland, two of the biggest energy companies in CEE, recorded mixed financial results in 2022 and 2023. Both benefited from strong oil and gas prices in 2022, which boosted their profits. However, they also face a number of challenges in 2023, including the ongoing war in Ukraine and the need to transition to a low-carbon economy.

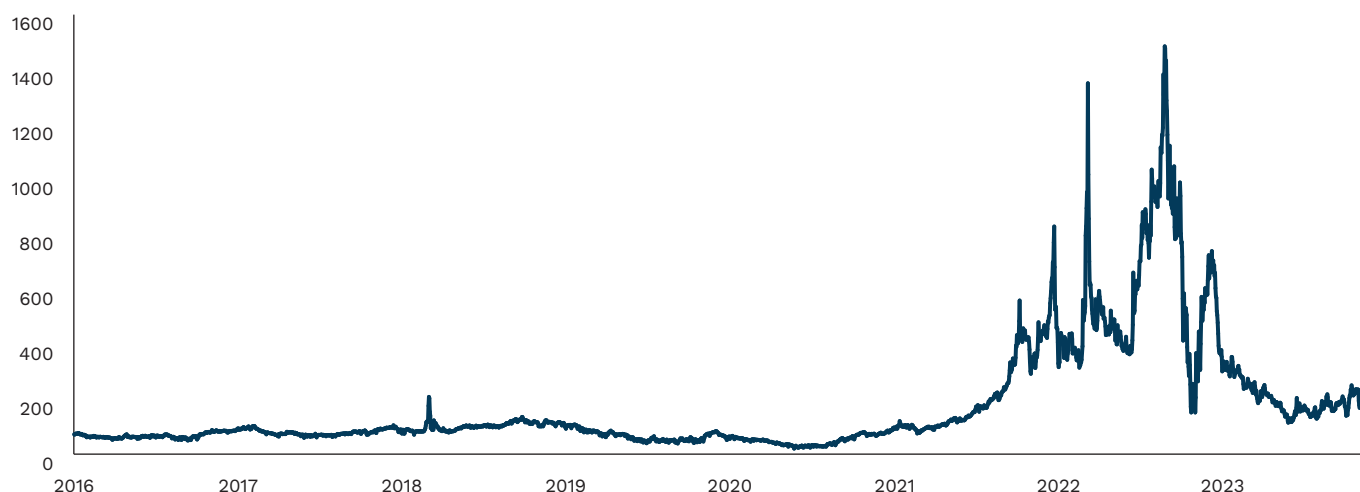
► **Lower oil and gas prices in 2023 led to a decline in revenue and profits in the energy sector.**

Since gas prices reached record highs in 2022, many consumers reduced their gas consumption or switched to alternative energy sources. The lower demand for gas led to a drop in gas prices in 2023. Gas prices have fallen to USD 40 per MMBtu as of October 2023. While still considerably higher than before the pandemic, they are much lower than the record highs earlier.

► **In 2023, MOL Group and PKN Orlen achieved varying financial outcomes influenced by market conditions.**

In its Q2 2023 report, the MOL Group, recorded a CCS EBITDA of USD 411 million, shaped by external market factors and government interventions, including substantial levies. The Hungarian company's financial performance was also affected by a new revenue-based extra tax, amounting to USD 315 million for the full year, which was recognised as a one-off expense. Despite these challenges, MOL Group's Consumer Services segment grew significantly in Q2, contributing nearly 43% of the total EBITDA, and somewhat offsetting the negative external factors. For 2023 as a whole, MOL Group has set its EBITDA guidance at around USD 2.5 billion. PKN Orlen's revenue in Q3 2023 amounted to PLN 75,424 million, with an EBITDA LIFO of PLN 8,220 million and a net result of PLN 3,459 million.

Figure 3.1. Gas prices (TGEgasDA, PLN/MWh)

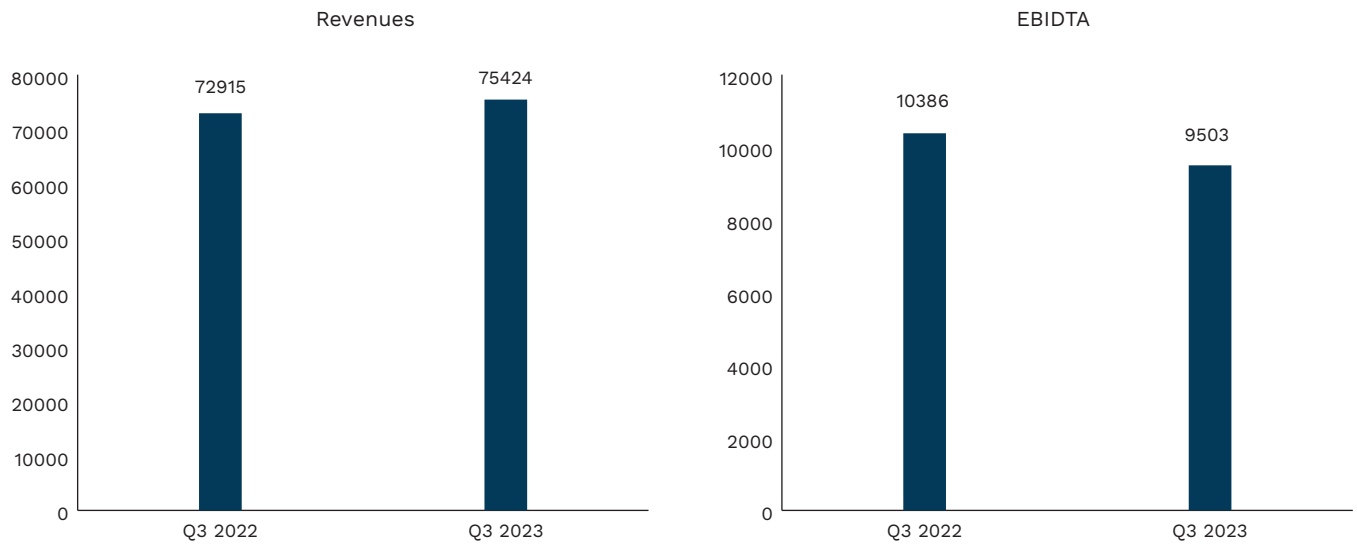


Source: TGE.

► **Credit rating agencies have responded to these financial results and broader market conditions.**

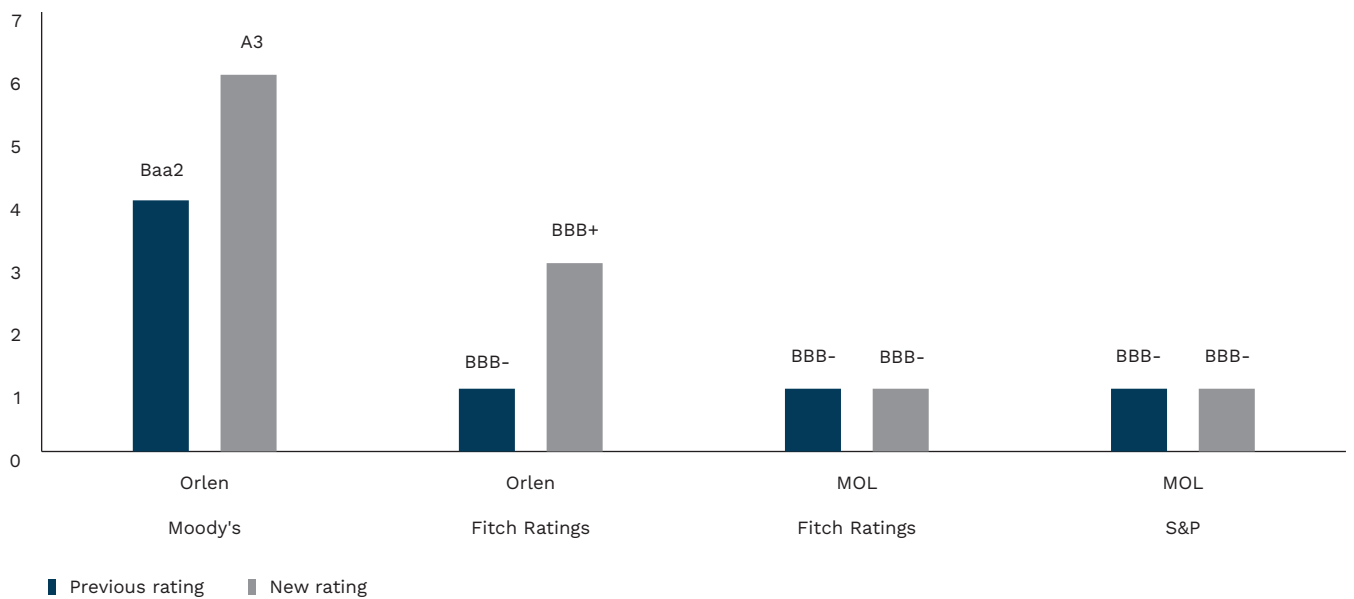
PKN Orlen's rating was upgraded by Moody's (from Baa2 to Baa1), Fitch Ratings (from BBB- to BBB+) and EuroRating (from BBB to BBB+), reflecting their positive assessment of its financial stability and strategic initiatives. Conversely, MOL Group's ratings has remained stable, with Fitch Ratings upholding its BBB- rating and S&P Global Ratings maintaining its existing ratings, indicating a steady performance amid market uncertainty, particularly in oil and gas supply.

Figure 3.2. Orlen's revenue and EBIDTA (PLN thousands)



Source: Orlen.pl.

Figure 3.3. Credit ratings of Orlen and MOL



Source: Moody's, Orlen, Fitch, S&P.

National policies to shield companies in Germany and CEE

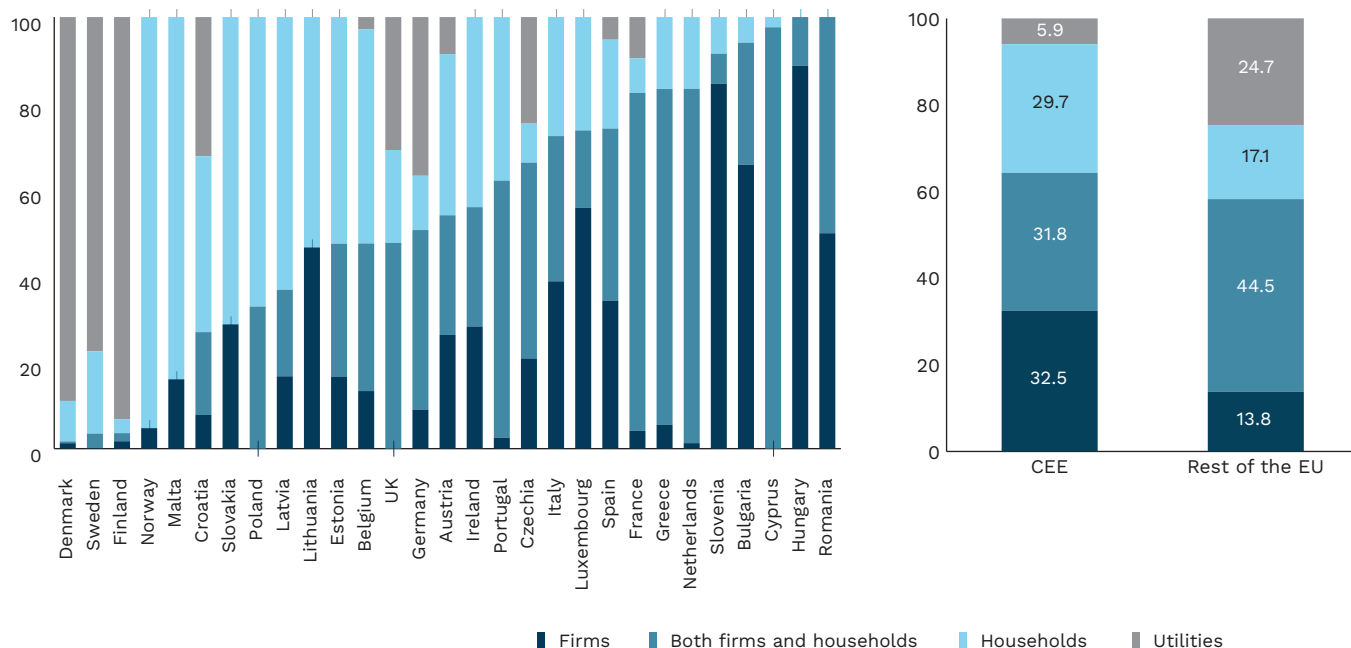
EUR 32.5 billion

Amount spent by CEE countries on shielding firms between September 2021 and January 2023, 64% of total spending to shield consumers from the energy crisis

► **European governments have tried to shield consumers and companies from the unprecedented energy price increases.** Hundreds of billions have been spent on freezing electricity or gas prices, reducing energy taxes, or thermal modernisation projects. Consumer support is likely to be concluded soon, but the lower the energy price, the better it is for the economy’s competitiveness. Germany has announced that it will lower energy prices for companies. We investigate whether CEE countries’ policies will support industry, too.

► **Between September 2021 and January 2023, CEE countries focused on companies while the rest of the EU focused on energy suppliers.** CEE countries spent EUR 16.4 billion on companies alone and EUR 16.1 billion on measures for both companies and households. 33% of total spending in CEE went to companies, compared to 14% in the rest of the EU. Meanwhile, the rest of the EU spent EUR 161 billion (25% of total spending) on utilities, helping them meet their liquidity needs through loans, bailouts and full nationalisation. In 2023, it has still been necessary for EU countries to support domestic industry by lowering energy prices to boost local competitiveness.

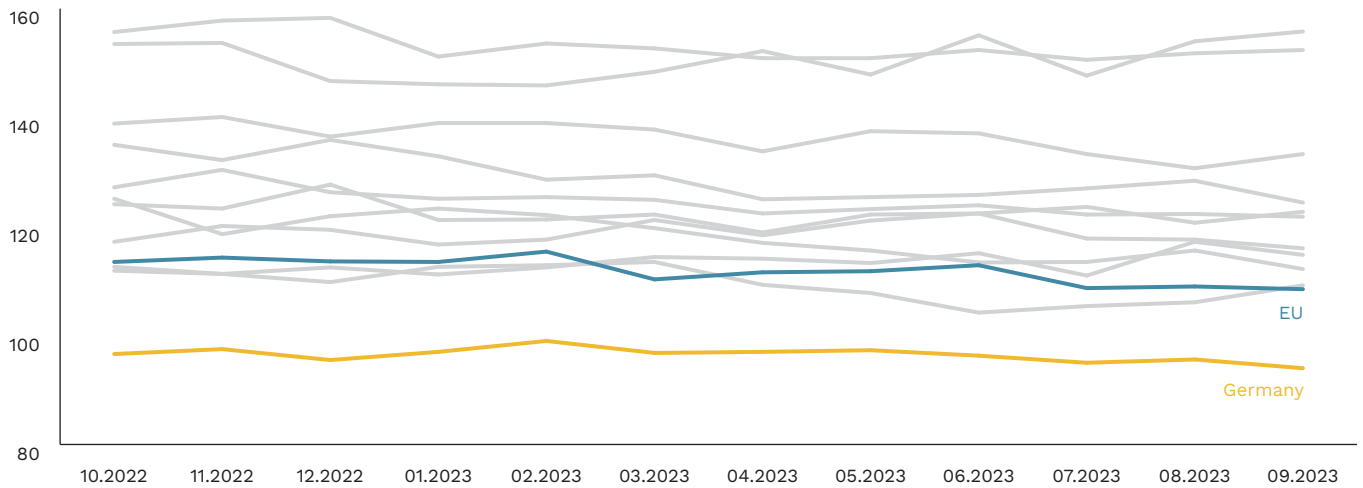
Figure 4.1. Governments’ earmarked and allocated funding to shield consumers from the energy crisis between September IX 2021 and January 2023 (%)



Note: the CEE countries are Bulgaria, Czechia, Estonia, Hungary, Lithuania, Latvia, Poland, Romania, Slovenia and Slovakia. By “utilities”, we mean measures targeting energy suppliers.

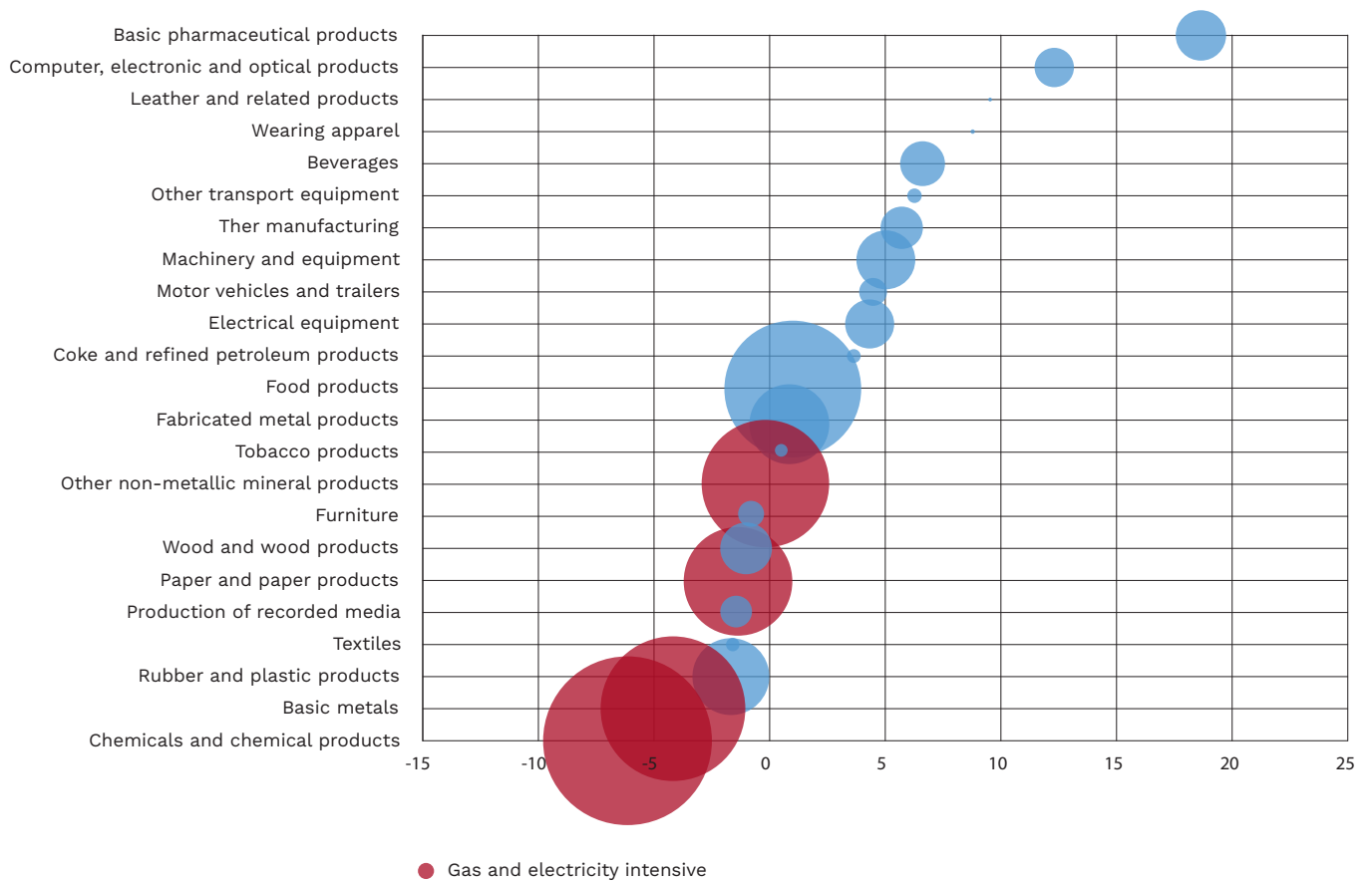
Source: Bruegel.

Figure 4.2. Production in industry – manufacturing (index, 2015=100)



Note: yellow denotes Germany, blue the EU, and grey CEE.
Source: Eurostat.

Figure 4.3. Change in production in the EU energy intensity manufacturing in 2022 (% y/y)



Note: size of the bubble is dependent on the energy consumption of the sector.
Source: Eurostat.

EUR 12 billion

value of the measures in the new German package for industry in 2024.

-6.1% y/y

– change in output of chemicals and chemical products industry (the most energy-intensive industry) in the EU in 2022

► **The German government has reached an agreement on a EUR 12 billion package of measures to support industry over the next year.** In total, the measures are for five years. The high electricity prices are making European companies relocate to countries with lower production costs. Germany has proposed to cut the electricity tax for all manufacturers to the minimum level permitted by EU law and to raise and extend for five years the compensation for 350 firms that compete internationally and are most at risk of relocating. Over the past year, production in German manufacturing has slowed down; in September 2023, was 6% lower than in 2015. German industry is performing worse than industry in the CEE countries.

► **CEE countries have not made plans to continue supporting industry in 2024 yet.** Continuing previous shields is expensive, but the more energy-intensive industries were (such as chemical and metals production), the more they reduced output in 2022 year on year. However, the price cap for electricity and gas in Czechia will end in December 2023; prices could increase by 10% next year. In Poland, electricity rates in 2024 will probably fall compared to 2023, but with the full unfreezing of electricity prices, consumer bills will increase significantly. Meanwhile, Hungary already plans to lower its wholesale gross list prices of motor fuels, reducing costs for both households and firms. Lack of support for industry in CEE – and in the EU overall – would harm Europe’s competitiveness on the global market and could extend the stagnation of the European market.

Discussion: The impact of the energy shock on German Industry

► Energy-intensive industry in Germany is facing a challenge due to the higher energy prices in Europe. Historically, German companies' energy efficiency has meant that more expensive energy has not been a significant problem. However, the current energy crisis has widened the gap between energy prices in Germany and those in economies outside Europe. The decline in Germany's competitiveness is raising concerns about deindustrialisation, particularly within energy-intensive industries.

► **Industries with high energy consumption tend to produce goods that mark the beginning of the production chain, especially in the domestic market.** For this reason, they play a crucial role in the German industrial landscape. The [German Economic Institute \(IW\)](#) highlights that 87% of the goods produced by these industries are destined for the domestic market, in stark contrast with the overall average in industry of 55%. Lower production in these sectors disrupts the entire value chain, potentially affecting other industries that depend on them, such as the automotive sector.

► **Although energy-intensive products play a key role in supply chains, they are often easy to substitute.** This implies that German energy-intensive industries have a limited ability to transfer costs to consumers due to the ease with which consumers can substitute their products with those of competitors. Nevertheless, a reduction in production in energy-intensive industries would not harm other industries significantly. [The ifo Institute](#) notes that products seen as gas-intensive, but which can easily be imported, are primarily concentrated in the chemical industry. In contrast, the largest share of gas-intensive products that are difficult to substitute is in the paper industry. The ifo analysis suggests that substituting easily substitutable products would reduce gas consumption by a quarter, with just a 2% decrease in the value added of German industry.

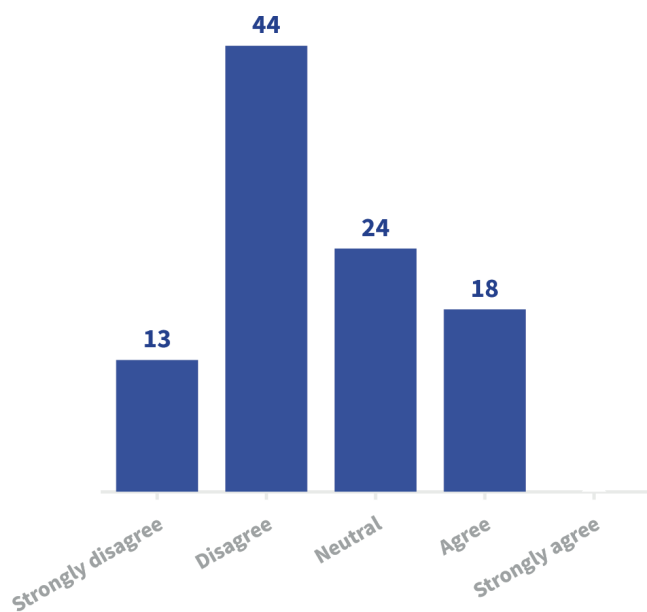
► **The challenge faced by energy-intensive industries is not merely a temporary issue; rather, it signifies a structural transformation.** The [German Economic Institute \(IW\)](#) highlights that gross fixed assets in energy-intensive industries have contracted by 19.7% since 2000. In contrast, the capital of non-energy-intensive industries has grown by 13.1%. As a result, overall gross fixed assets in manufacturing have grown moderately (by 5.3%). IW suggests that the expected higher energy prices in the future, especially compared to non-EU economies, have been the primary factor limiting investment in these industries. The energy crisis of 2022 has further cast doubts on German competitiveness. Consequently, the subdued production in this sector does not point to more optimistic investor sentiment, potentially leading to further contraction in capital.

► **The appropriateness of the German government's financial support for industries affected by energy prices is a matter of ambiguity.** [The ifo Institute](#) suggests that even if prices were to revert to the same levels as before Russia invaded Ukraine, the persistent political uncertainty linked to energy prices would remain high. In such a scenario, government intervention becomes crucial to enable competitive companies to continue producing in Germany. Conversely, [CEPR](#) argues that policymakers should refrain from impeding the transition unless strategic industries are directly affected. Subsidising energy prices may not be cost-effective in the long run and resisting structural change could result in higher future costs.

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Inflation rates of 3-4 percent will be the new normal.
(% of respondents)



Source: Polish Economic Institute and IfW Kiel.
Survey conducted from 29 Mar to 14 Apr. Sample includes 45 responses

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Contact
Jakub Rybacki
Head of the Macroeconomics Team
jakub.rybacki@pie.net.pl
phone: 48 512 275 365