Political divisions in Poland create an unfavourable policy environment

Poland's post-election political landscape remains fragmented, following the victory of opposition candidate Karol Nawrocki over Rafał Trzaskowski, who was backed by the incumbent ruling coalition. GDP growth prospects remain unchanged, but the country's policy mix may be unfavourable with loose fiscal measures and restrictive monetary policy

Polish President-elect Karol Nawrocki

Opposition candidate Karol Nawrocki's victory in the presidential elections earlier this month means that the political gridlock will continue, and the political scene should remain highly polarised, which means continued loose fiscal and restrictive monetary policy. The short-term economic growth prospects remain unchanged after the elections.

Following somewhat softer first-quarter GDP (up by 3.2% YoY vs 3.4% YoY in 4Q24), the first set of second-quarter monthly data points to an acceleration in economic growth. Both retail sales and industrial output came in higher than expected, and these stronger readings should continue for the remainder of the quarter. The composition of first-quarter growth became more balanced as consumption growth (up by 2.5% YoY) was accompanied by a rebound in fixed investment (6.3%

YoY).

Both headline and core inflation continued to decline in May, with prints below market consensus. The decision to cut natural gas regulated prices for households from July by nearly 15% (the gas bill by 10%) also improved the inflationary outlook. We see CPI inflation dropping below the National Bank of Poland (NBP) target of 2.5% in the second half of 2025. But the NBP doesn't share our 'inflation optimism'. The Monetary Policy Council (MPC) held rates as expected in June, but the rhetoric has turned more hawkish again, pointing at fundamental factors that could drive inflation high over the medium term.

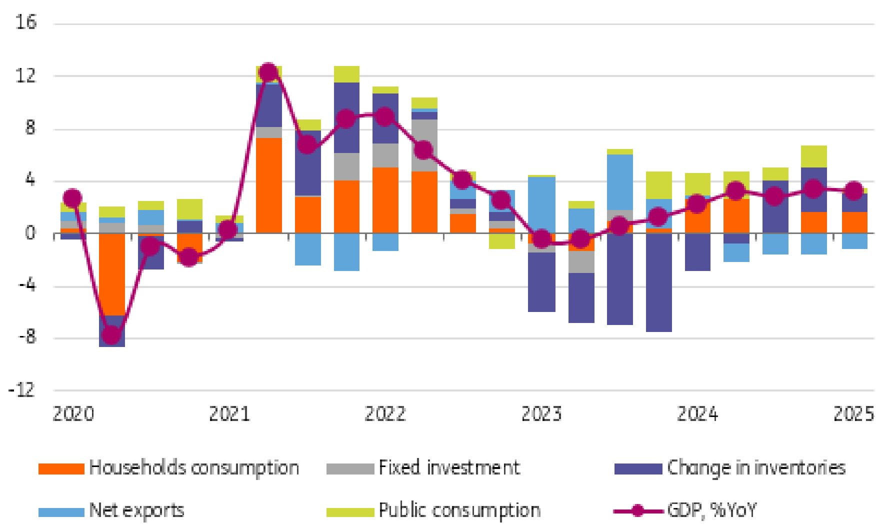
We revert to our earlier projection for NBP rates, of a terminal rate of 4.25% instead of 3.75%. This would imply an ex-ante real rate just below 2%, aligning closely with the NBP's estimate of the neutral rate.

Economic growth composition improved in the first quarter

Despite economic growth easing to 3.2% YoY in 1Q25 from 3.4% YoY in 4Q24, the composition of GDP actually improved, pointing to more balanced and diversified sources of growth. Private consumption remained the main engine of GDP expansion, while fixed investment rebounded after declines in the second half of last year. Investment was most likely concentrated in the public sector (potentially military equipment). High-frequency data suggest that growth momentum improved in early 2Q25.

Poland remains on course to achieve economic growth above 3% this year, outperforming CEE peers and other EU member states. Real convergence continues and Poland is gradually closing the income gap versus the EU.

Real GDP (%YoY) and contributions (ppt)



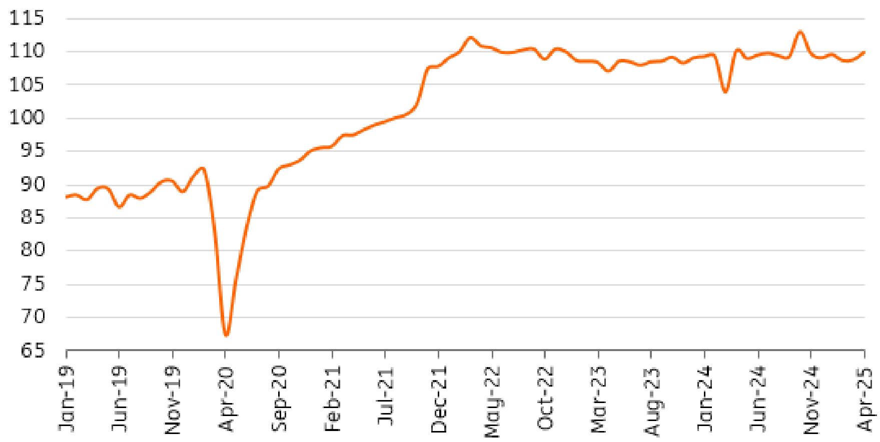
Source: GUS, ING.

High uncertainty weighs on manufacturing

Although manufacturing activity has shown encouraging signs in recent months, the sharp decline in manufacturing PMI in May warrants a cautious approach when evaluating the industrial output outlook.

Global trade uncertainty remains elevated amid unpredictable US trade policy. It cannot be ruled out that the recent improvement in demand for Polish manufacturing goods was linked to the frontloading of orders ahead of higher US tariffs. In May, purchasing managers reported a substantial deterioration in demand.

Manufacturing output, 2021=100, SA



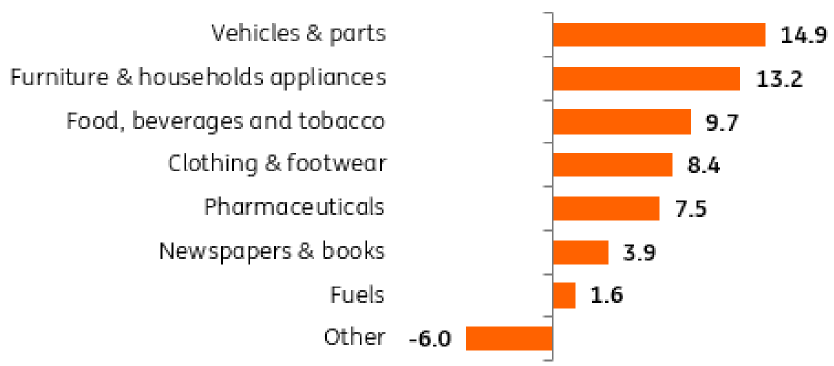
Source: GUS

Demand for durable goods continues to improve

Retail sales volatility in March and April was mainly driven by the calendar effect (different timings for the Easter holiday in 2024 and 2025), but positive trends emerged in the sales of durable goods, including cars, furniture, electronics and household appliances.

Similar to developments in manufacturing, it is yet to be seen whether it marks the beginning of a more profound recovery in consumer demand. It may merely reflect advanced purchases ahead of potentially higher tariffs on goods imported from Asia and cars. Still, consumer demand remains solid, especially for services.

Retail sales (real), April 2025 (%YoY)



Source: GUS, ING.

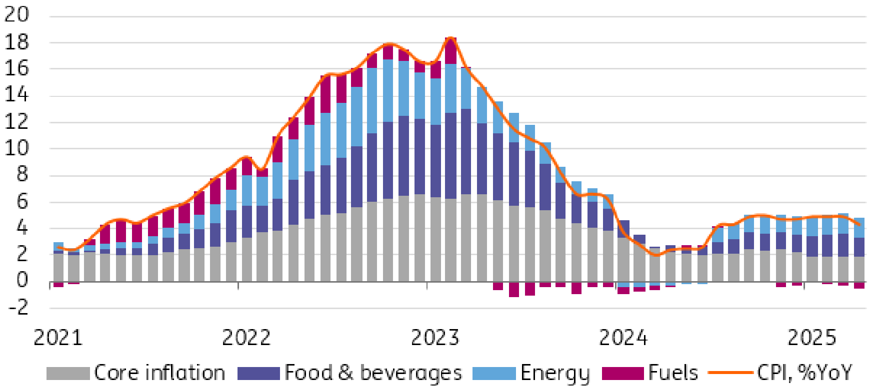
CPI and core inflation continue downward trend

According to the flash estimate, CPI inflation eased to 4.1% YoY in May from 4.3% YoY in April, surprising to the downside. Partial data suggest a further decline in core inflation, excluding food and energy prices as well.

The inflation outlook continues to improve. The Energy Regulatory Office (URE) decision to cut the official tariff for regulated gas prices should reduce the average gas bill for households by about 10% from July.

Headline CPI inflation should decline well below 3% YoY in July and remain close to the National Bank of Poland's target of 2.5% in the second half of this year.

CPI inflation, %YoY, percentage points



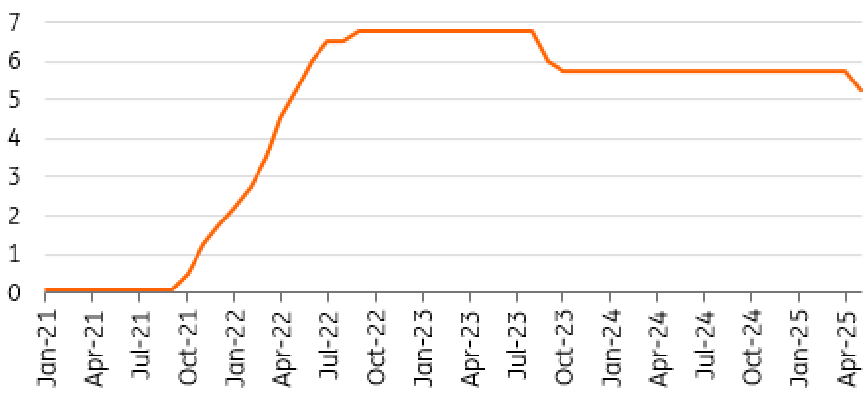
Source: GUS

NBP doesn’t share our ‘inflation optimism’

The MPC cut rates by 50bp in May as inflation was running below the path outlined in the NBP macroeconomic projection at the beginning of 2025. This deviation was partly driven by the annual revision of CPI basket weights and a continued decline in core inflation.

Headline inflation keeps surprising to the downside, while core inflation maintains the downward path. But the NBP doesn’t share our ‘inflation optimism’. The MPC held rates as expected in June, but the rhetoric has turned more hawkish again, pointing at fundamental factors that could drive inflation high over the medium term.

NBP reference rate (%)



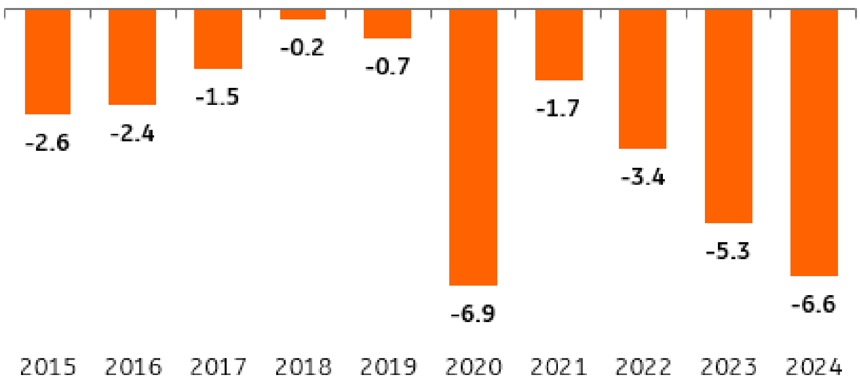
Source: NBP

Unfavourable starting point for fiscal adjustment

In 2024, the fiscal outcome turned out worse than expected, and the general government deficit amounted to 6.6% of GDP. In 2025, the Polish authorities expect the fiscal gap to still be in excess of 6% of GDP. That means that Poland has a lot of fiscal ground to cover to put an end to excessive deficit by 2028, even taking into account the national exit clause linked to the Re-Arm EU initiative that allows for special treatment of defence spending.

The victory of Karol Narwocki in the presidential elections makes fiscal austerity even more challenging as he may veto consolidation measures. At the same time, the ruling coalition may be inclined to deliver new costly fiscal pledges ahead of the 2027 parliamentary elections. We expect the new spending to be spread over time as much a possible, or the delivery of the most costly pledges to be lagged.

General government balance (% of GDP)



Source: Ministry of Finance

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