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POLAND

Poland's economic rebound in doubt as industry slows

Following better-than-expected first-quarter GDP, manufacturing data suggest the second quarter started on a weak note. This year, net exports should be the flywheel of the Polish economy. The labour market remains solid, but wages have been failing to catch up with inflation for months



Poor manufacturing activity

Industrial production fell by 6.4% year-on-year in April (ING forecast: -2.5%; consensus: -3.3%), following a 3.1% YoY decline in March (revised), the third consecutive month of decline in annual terms. Seasonally adjusted output fell by 1.6% month-on-month.

The decline in industrial activity was broad-based last month. Manufacturing output fell by 5.6% YoY, but we also saw declines in mining (-11.7% YoY) and power generation (-14.3% YoY).

The weakness in manufacturing can be attributed to falling orders from European industry and the normalisation of input inventories built up in previous quarters. There is also a gradual fading of the post-pandemic boom in the automotive industry, which recovered from the 2022-23 production slump after supply chains eased. We have also observed slower activity

growth in the food industry, which rebounded strongly a year ago after the start of the war in Ukraine.

Among the manufacturing divisions, the deepest year-on-year declines were seen in the production of chemical products (-23.0%), metals (-16.6%) and non-metallic mineral products (-15.7%). The largest increases were recorded in the repair, maintenance and installation of machinery and equipment (+32.1%) and their manufacture (+12.0%).

Producer prices slow

Producer price inflation (PPI) slowed to 6.8% YoY in April (ING: 6.8%; consensus: 7.0%) from 10.3% YoY a month earlier (data revised). PPI inflation fell to single-digit levels for the first time since mid-2021. The PPI index declined for the fourth consecutive month in month-on-month terms, with manufacturing prices moderating continuously since November last year.

Given the correlation (with a lag) between PPI and CPI, we expect a further decline in consumer prices in the coming months. However, it will be noticeably slower due to adjustments in firms' costs to the earlier shock in the commodity market, including energy and wage pressures.

Labour market strong despite poor economic conditions

In April, average wages in the corporate sector rose by 12.1% YoY, compared to a 12.6% YoY increase in March. The result was in line with the market consensus.

Growth in employment slowed to 0.4% YoY (consensus: 0.3%) from 0.5% YoY a month earlier. But seasonally adjusted month-on-month changes in employment improved after a weaker first quarter.

So, the labour market remains tight despite signs of cooling in trade, transportation, administration and some manufacturing divisions seen in late March.

In the face of high inflation, this translates into continued robust nominal wage growth. The next increase in the minimum wage is coming in the summer, so second-quarter wage data may be somewhat slower as firms accumulate budgets for the coming wage hikes.

However, salaries have been growing slower than inflation for months, resulting in a decline in the real purchasing power of Polish consumers. This trend is unlikely to change for most of the year. The result will be stagnation or a slight decline in real household spending.

The bottom line

Data for industry point to a strong deceleration in output and a further marked slowdown in producers' price pressures, raising concerns about the strength of the rebound in the second quarter. Although first quarter GDP turned out better than expected, and business surveys

suggest an improvement in the following quarters, today's data paint a less optimistic picture for the start of the second quarter.

In 2023, net exports may be the main driver of the Polish economy. So weakening industry is a concern, but on the other hand, we see quite mixed expectations for the economy of Poland's main trading partner, Germany. They are ranging from a very pessimistic one that the slowdown will deepen in the second half of the year to a more optimistic one that assumes that the recent industrial slowdown is related to overbuilt inventories, while a gradual improvement in China will help German industry and the services sector will maintain its strength. We still believe that the bottom of the business cycle will come in the first half of 2023, but the recovery may be sluggish.

We are concerned that tomorrow's retail data will also confirm the low level of economic activity in April. Against this backdrop, the labour market remains in a relatively solid shape, which may slow the pace of the decline in core inflation. With the expiry of the commodity and energy shock, companies are increasingly pointing to cost pressures from rising labour costs.

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