

Economic forecast for 2022: Back to the old growth path

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Executive Summary

- During 2021, Ukraine's economy has been recovering from demand and supply shocks resulting from lockdowns due to the pandemic
- However, several COVID waves, production constraints, and logistical limitations in real exports negatively affect the recovery path
- As a result, we estimate a **2.8%** real GDP increase for **2021**
 - Strong positive contribution of private consumption
 - Recovery of investment
 - Strong negative contribution of net exports
- For **2022**, we forecast real GDP to increase by a relatively moderate **3.3%**
 - Strong agricultural harvest of 2021 to be visible in the export recovery of 2022
 - Continuation of private consumption growth
 - Broad-based recovery of industry and services on the supply side
- **Thus, the pre-crisis level of real GDP will be only reached and crossed in 2022**
- **Overall, we forecast Ukraine to be back on its pre-crisis growth rate in 2022**
- **This implies a moderate path of economic development**

Structure

1. Motivation
2. Review: Real GDP in 2021
3. Assumptions for 2022
4. Forecast for 2022:
 - Real GDP
 - GDP demand and production sides
 - Inflation
 - Current account
5. Key risks of the forecast

Contact

Annex

1. Motivation

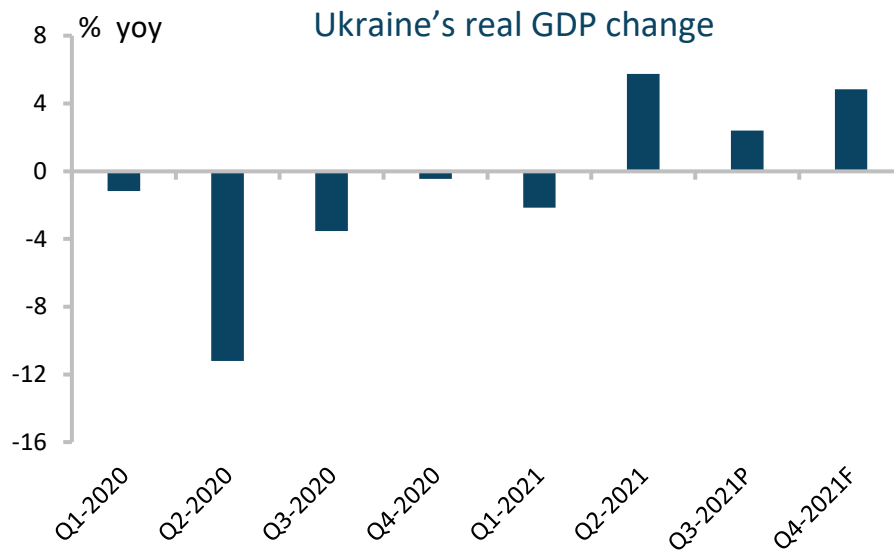
Background:

- In 2021, Ukraine's economy is on the recovery path from the decline in 2020 caused by the COVID-19 pandemic
- However, as the pandemic continues to affect countries around the globe, economic uncertainty remains exceptionally high
- Therefore, economic forecasting is needed more than ever, but subject to significant risks

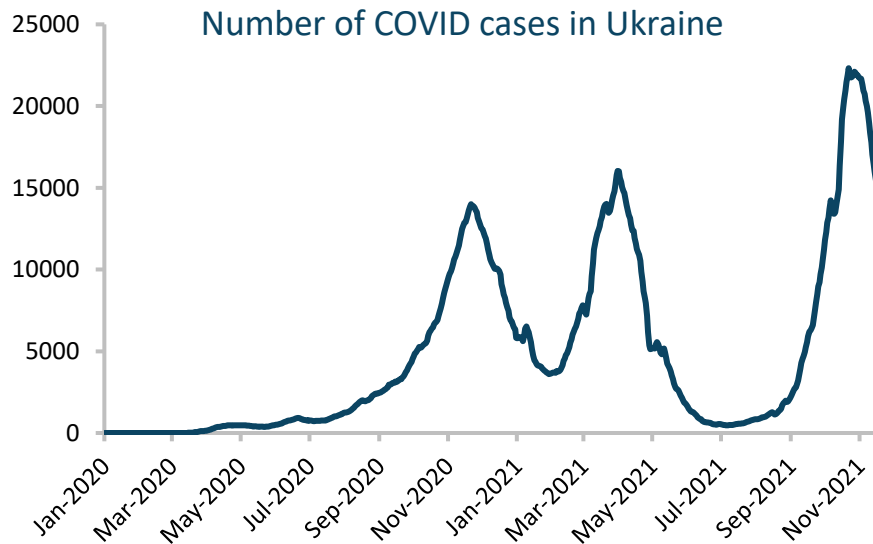
Purposes of this Policy Briefing:

- Assess Ukraine's economic performance in 2021 amid the recovery from the COVID-19 pandemic
- Present the forecast of key macroeconomic parameters for 2022
- Discuss main risks of the forecast

2. Review: Real GDP in 2021



Source: Ukrstat; Own forecast

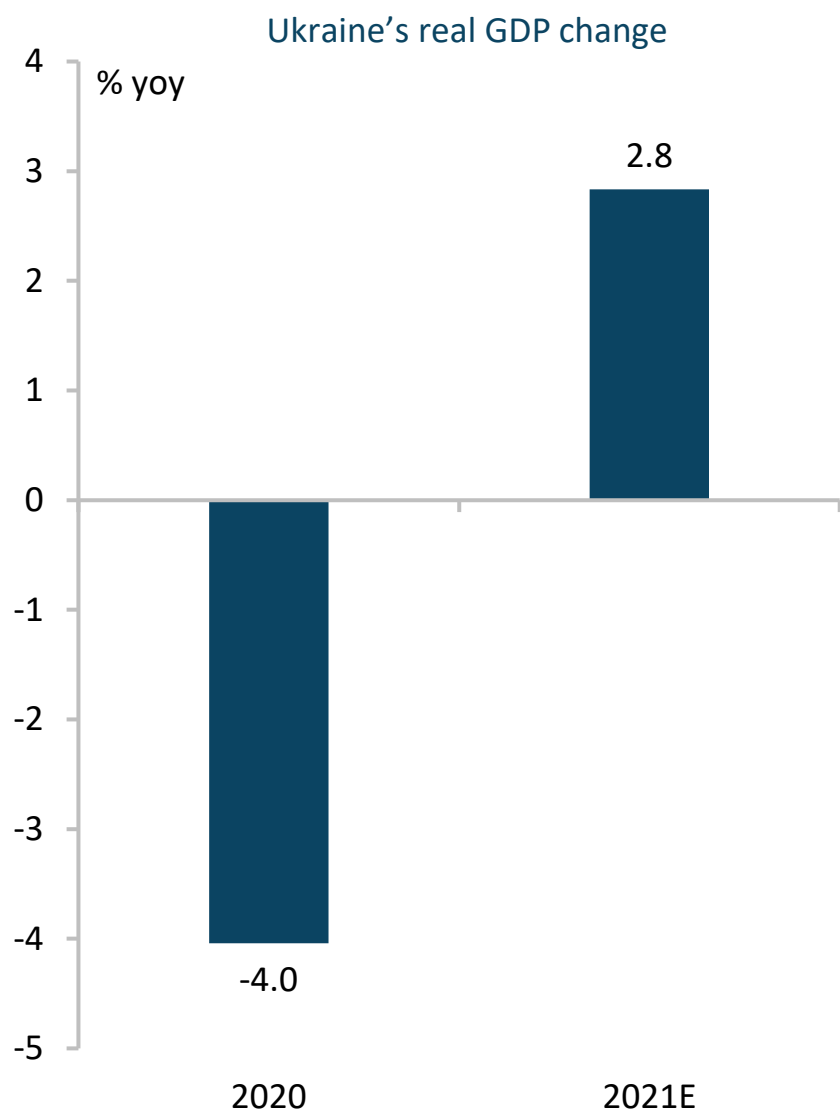


Source: WHO Note: 7-day moving average

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- Economic dynamics were very uneven during 2021
- In the first half of 2021, the economy performed below expectations:
 - Second wave of COVID cases limited recovery of investment and increased restrictions on economic activity
 - Exports fell in real terms
- In the second half of 2021, there are signs of improvement:
 - Recovery of investment and export volumes
 - But resurgence of COVID dampens growth prospects
- Reports of a record harvest add to growth estimates in Q4

Review: Real GDP in 2021 (cont'd)



Source: Ukrstat for 2020, own estimate for 2021

Real GDP change:

- Jan-21 estimate: 4.2% growth in 2021
- Dec-21 estimate: 2.8% growth in 2021 after drop by 4.0% in 2020
- **Real exports declined even as external demand was stronger than expected**
- **Consumption stronger than expected offsetting effects of weak imports**

Why?

- Exporters failed to use the opportunities in full: restricted production capacities in metallurgy
- Logistical limitations delayed exports of the new harvest

3. Assumptions for 2022: Domestic

- **Intensive fighting in Donbas does not restart** within the forecasting period as the current geopolitical tensions do not escalate
- **Quarantine restrictions** in some form will continue through 2021 and 2022 as new virus variants emerge and vaccination progress is limited
- **Cooperation with IMF and other development partners continue** in response to progress in key areas including rule of law, anti-corruption institutions, public finance management, monetary policy, public administration, energy policy
- **One disbursement from IMF Stand-by Arrangement** (at USD 700 m) is expected by the end of the programme
- **Access to global financial markets** will be maintained
- The **NBU will keep monetary policy tight** to return inflation to target
- **Financial sector will remain stable** in 2022 with some expansion of lending
- **Tax rates** remain unchanged

Assumptions for 2022: External

GDP growth in major economies, % yoy

	2020	2021	2022
USA	-3.4	5.9	4.0
EU	-6.0	4.8	4.2
China	2.3	8.2	5.4
Russia	3.0	4.2	2.6
Turkey	1.8	8.3	4.0
India	-7.3	9.0	7.6

Source: FocusEconomics consensus forecast, November 2021 edition;
Fitch solutions global macro forecast, January 2022

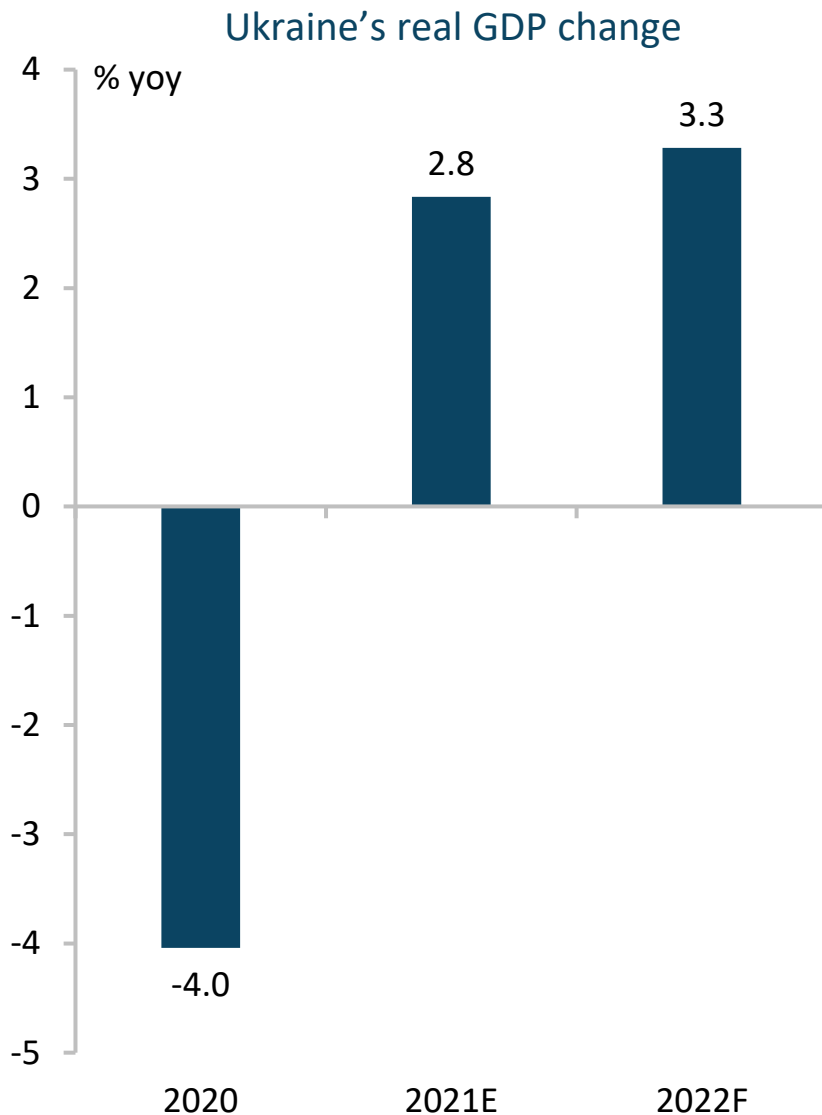
2021/2022 key commodity prices

	2020	2021
Wheat (USD/tonne)	296	297
Corn (USD/tonne)	270	256
China Steel HRC (RMB/tonne)	5349	5156
Iron ore (USD/tonne)	161	93
oil Brent (USD/barrel)	72	67

Sources: Oxford Economics, Economist Intelligence Unit

- Global shortages and high commodity prices will create a drag on economic growth in 2022
- Real GDP growth assumptions for key trading partners:
 - USA: +4.0%
 - EU: +4.2%
 - China: +5.4%
- Prices for key commodities in Ukraine's international trade will be lower on average in 2022 but will remain close to levels in Q4-2021

4. Forecast for 2022: real GDP



Source: Ukrstat for 2019, own estimates for 2021 and forecast for 2022

Key GDP parameters for 2022:

- Real growth: +3.3%
- Nominal GDP: UAH 5,750 bn (USD 212 bn)
- **Real GDP slightly above 2019 level**

Key driving forces:

- Demand side: continued growth of private consumption stimulated by growing minimum wage and social payments
- Negative contribution of real net exports
- Supply side: broad-based recovery in industry and services

Forecast for 2021: demand side

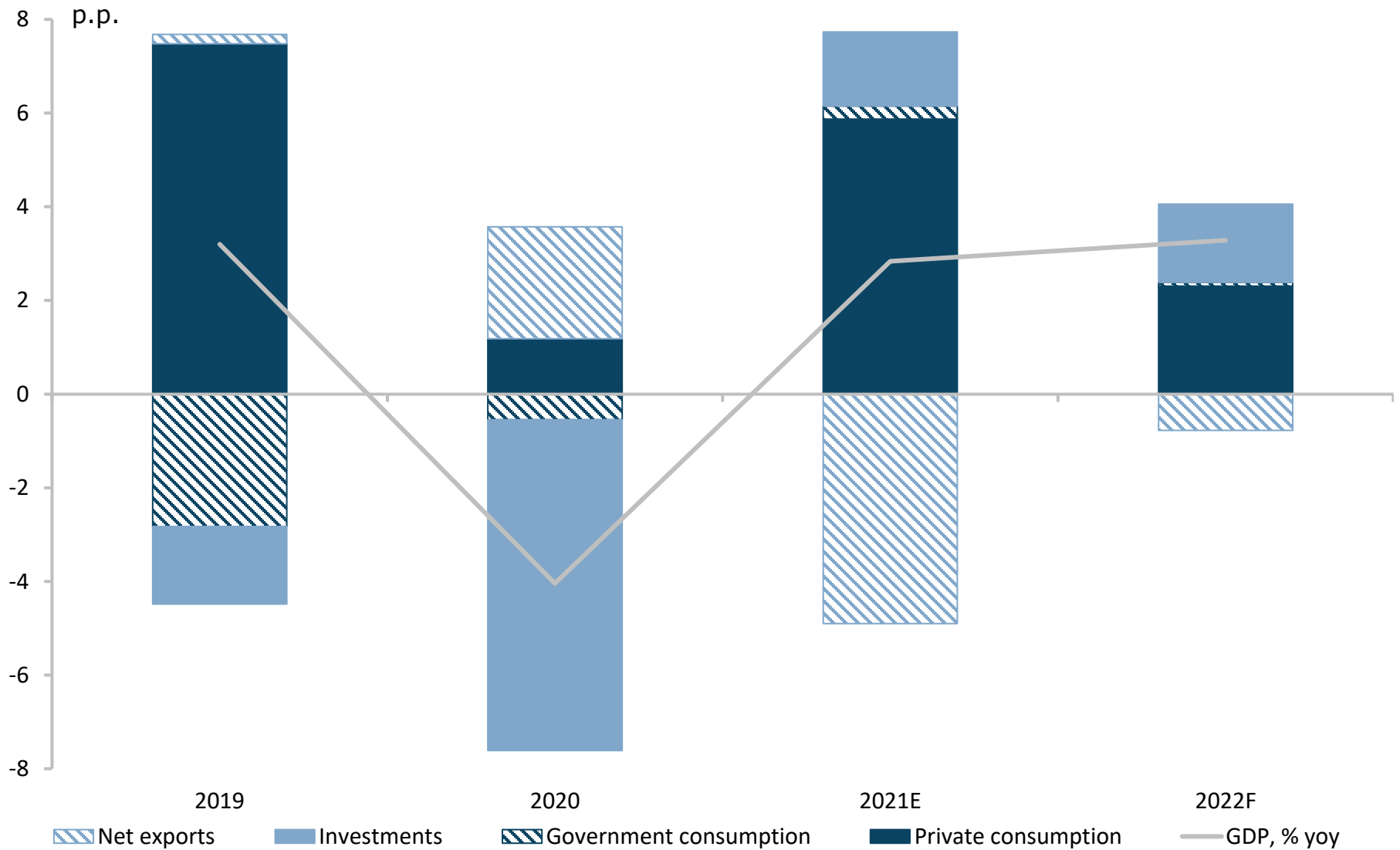
Real GDP forecast: demand side (change in %)

	2019	2020	2021E	2022F
GDP	3.2	-4.0	2.8	3.3
<i>Including</i>				
Private consumption	10.9	1.6	8.0	3.2
Government consumption	-13.6	-2.9	1.4	0.4
Fixed capital accumulation	11.7	-24.4	8.1	9.1
Exports	7.3	-5.6	-0.8	4.5
Imports	5.7	-9.5	11.4	6.3

Source: Ukrstat, own calculations

- Private consumption is expected to drive the economic recovery in 2021 and 2022
- Real exports will slightly decline in 2021 as exporters faced difficulties in increasing production and expanding market share
- In 2022, exports will be supported by a record grain harvest
- Real imports surged after a drop in 2020
- The contribution of net real exports will be negative due to higher import growth

Forecast for 2021: contributions to real GDP growth



Source: own calculations; note: E – Estimate, F - forecast

Forecast for 2022: production side

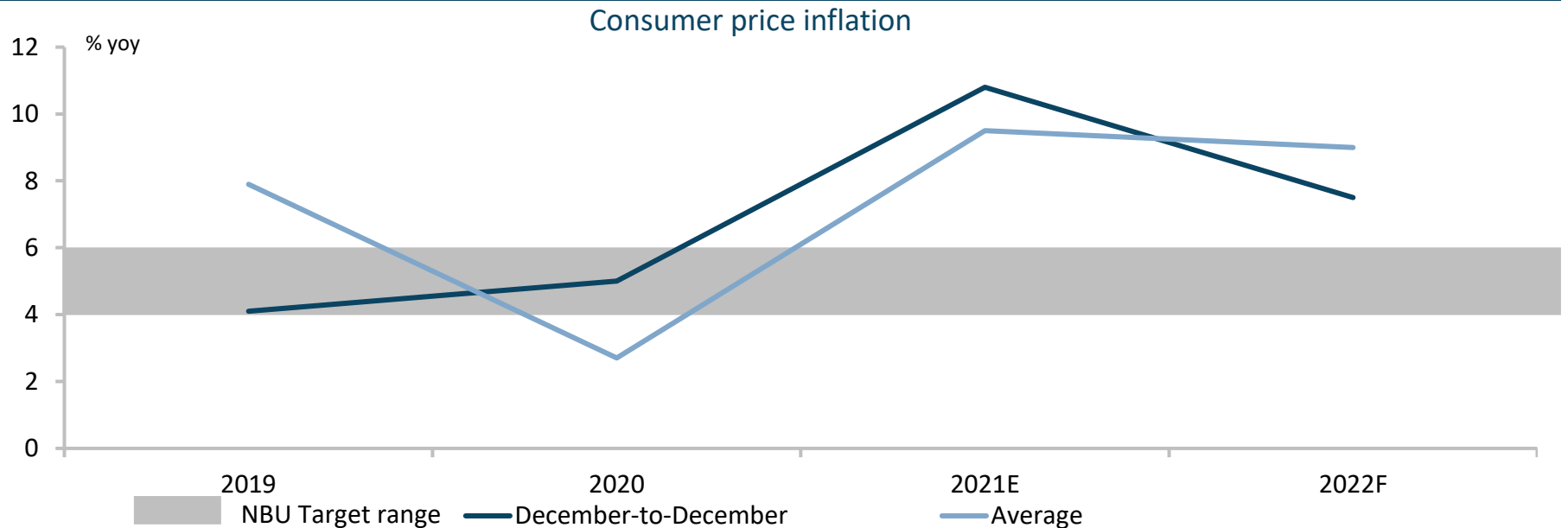
Real GDP forecast: supply side (change in %)

	2019	2020	2021E	2022F
GDP	3.2	-4.0	2.8	3.3
<i>including</i>				
Agriculture	1.0	-11.5	11.9	0.8
Industry	-0.6	-4.4	1.7	2.9
Trade	3.5	4.8	1.8	4.5
Transport	3.9	-16.4	1.2	5.9

Source: Ukrstat, own calculations

- Agriculture is expected to surge in 2021 due to a record grain harvest and slight growth is forecast for 2022
- Recovery in industry and trade is expected to be supported by stronger external and domestic demand
- Economic activity in transport is projected to remain far lower than in 2019
- Recovery in services and construction is expected

Forecast for 2022: inflation



Source: Ukrstat, own calculations

- Domestic demand and higher import prices contribute to inflation pressure
- Stronger exchange rate so far helped moderate inflation
- The NBU tightened policy rate and committed to keeping monetary policy tight enough to bring inflation closer to target
- Inflation expectations are expected to remain anchored in 2022 while external price pressure is expected to decline
- But expected increases in administrative prices after price caps in 2021

Forecast for 2021: current account

		Current account			
		2019	2020	2021E	2022F
Current account balance	USD bn	-4.1	6.2	-0.4	-3.6
Current account balance	% of GDP	-2.7	4.0	-0.2	-1.7
Exports of goods	USD bn	46.1	45.2	63.2	63.8
Imports of goods	USD bn	60.4	51.8	67.1	70.0
Balance of services	USD bn	1.8	4.8	4.1	2.9
Transfers and remittances	USD bn	19.2	15.3	18.1	19.3

Source: NBU, own calculations

- Increase in investment income transfers and trade balance deficit contribute to negative current account balance in both 2021 and 2022
- Nominal exports of goods in 2022 close to levels of 2021 due to drop in prices for some commodities, primarily iron ore
- Decline in energy prices as compared to autumn 2021 will restrict growth of nominal imports

5. Key risks of the forecast

Downside risks:

- **Escalation of conflict with Russia** will result in the sharp downturn of the economy, absence of access to the international capital market
- **More severe quarantine measures and lockdowns in Ukraine** will result in lower real private final consumption negatively affecting retail and services sectors
- **Failed cooperation with the IMF** as a result of an absence of necessary policy steps will again restrict the possibilities for the Government to attract concessional lending and limit fiscal space
- **Continuation of a global pandemic due to slow vaccination worldwide, and/or new virus variants appearing** will reduce external demand, affect global supply chains and increase uncertainty negatively, impacting Ukraine's economy
- **Political crisis in Ukraine** resulting in pre-term Parliamentary elections will result in higher uncertainty in the country and likely a new wave of populism

Upside risks:

- **Better consumer sentiment** in Ukraine amid slowdown of pandemic

About the German Economic Team



Financed by the Federal Ministry for Economic Affairs and Energy, the German Economic Team (GET) advises the governments of Ukraine, Belarus, Moldova, Kosovo, Armenia, Georgia and Uzbekistan on economic policy matters. Berlin Economics has been commissioned with the implementation of the consultancy.

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Annex: Technical note on modelling

- Forecast was produced using the IER short-term macroeconomic forecasting model. Model is based on iterative-analytical techniques, grounded in the system of national accounts
- Model looks at GDP and GDP components based on production and expenditures. The final result of the GDP forecast is based on forecasts for each component.
- The forecast for each component is produced using scenario assumptions and historical relationships. The forecast is built on a system of built-in proportions, which are expected to stay fairly constant
- Components of the GDPs by production and by expenditures are interconnected.
- The real GDP growth is determined by the summation of the contributions of each component. If the two sides of the GDP accounting equation are not balanced, then another iteration begins. The iterations continue until the two methods of GDP produce balanced results.

Annex: Forecast indicators

	2019	2020	2021E	2022F
Real Economy				
Nominal GDP, UAH bn	3 977	4 192	5 164	5 750
Nominal GDP, USD bn	153.9	155.5	189.7	212.0
Real GDP, % yoy	3.2	-4.0	2.8	3.3
Real disposable incomes, % yoy	8.4	2.6	5.9	4.6
GDP Deflator, % yoy	8.2	9.8	19.8	7.8
Consumer price index, aop, % yoy	7.9	2.7	9.5	9.0
Consumer price index eop, % yoy	4.1	5.0	10.8	7.5
Unemployment rate (ILO methodology), %	8.2	9.5	9.7	9.6
Fiscal sector				
Consolidated fiscal balance, % GDP	-2.2	-5.3	-3.8	-2.9
Consolidated fiscal debt (direct+guaranteed), % GDP	50.2	60.9	51.0	49.8
Balance of Payments				
Current account balance, % of GDP	-2.7	4.0	-0.2	-1.7
Exports of goods and services, % yoy	7.3	-5.6	-0.8	4.5
Imports of goods and services, % yoy	5.7	-9.5	11.4	6.3
Exchange rate (official), aop, UAH/USD	25.84	26.96	27.23	27.44