

Overview

- Russia`s full-scale war has been causing dramatic human and economic suffering. GDP is expected to decline by 32% yoy in 2022, the unemployment rate is currently at 35%
- Due to very high uncertainty, a comprehensive forecast for 2023 is hardly possible
- The war forced 6 m people to flee abroad and further 6 m are displaced within Ukraine as 20% of Ukraine`s area is occupied and economic damage recorded at USD 114 bn
- Public finances are strongly hit as the budget deficit stands at USD 5 bn per month
- Deficit is funded by NBU`s monetary financing and intern. support (grants and loans)
- The NBU introduced a fixed exchange rate regime and capital controls. A strong decline in reserves (USD 7 bn) necessitated a devaluation of the exchange rate in July
- CPI is expected to exceed 30% yoy in December
- Strong decline of foreign trade, blockage of seaports has global implications

Special topics

- **Financial aid.** Grants are preferred over loans to reduce future debt burden
- **Reconstruction.** Effort requires coordination to link support with reforms and investment
- **International food security.** Russia`s port blockage/destruction cause food instability to rise

Basic indicators

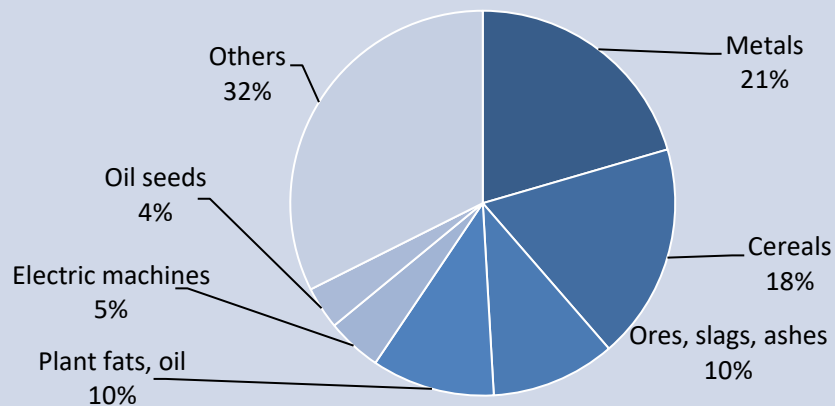
	Belarus	Russia	Ukraine	Moldova	Georgia
GDP, USD bn	68.2	1,775.5	200.3	13.7	18.7
GDP/capita, USD	7,295	12,198	4,838	5,285	5,014
Population, m	9.3	145.6	41.4	2.6	3.7

Sources: National statistics, IMF, GET/IER estimate, note: data for 2021

Trade structure

Exports

EU 39% | China 12% | Others 49%

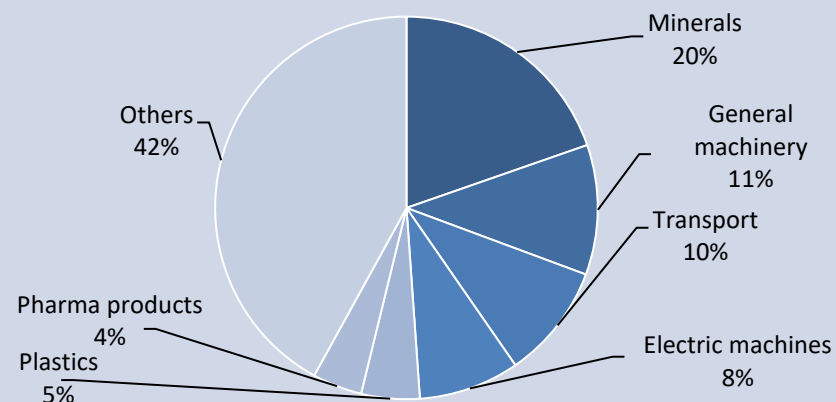


Source: Ukrstat, 2021; note: trade in goods

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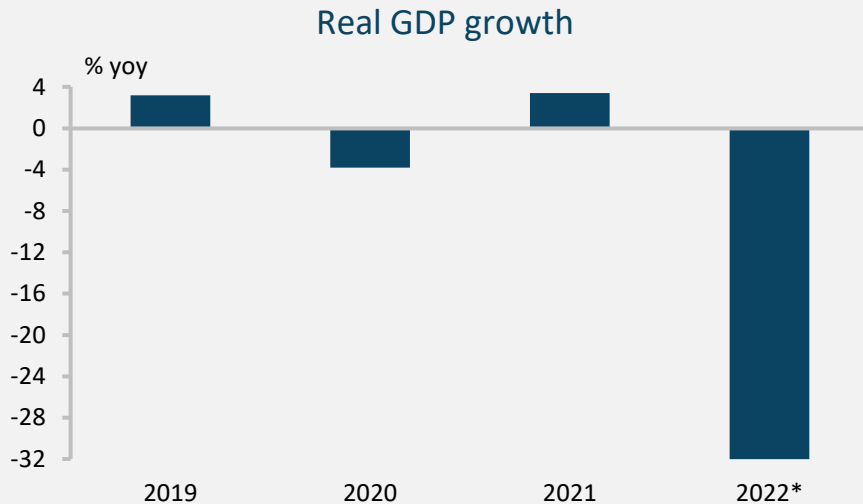
Imports

EU 40% | China 15% | Others 45%

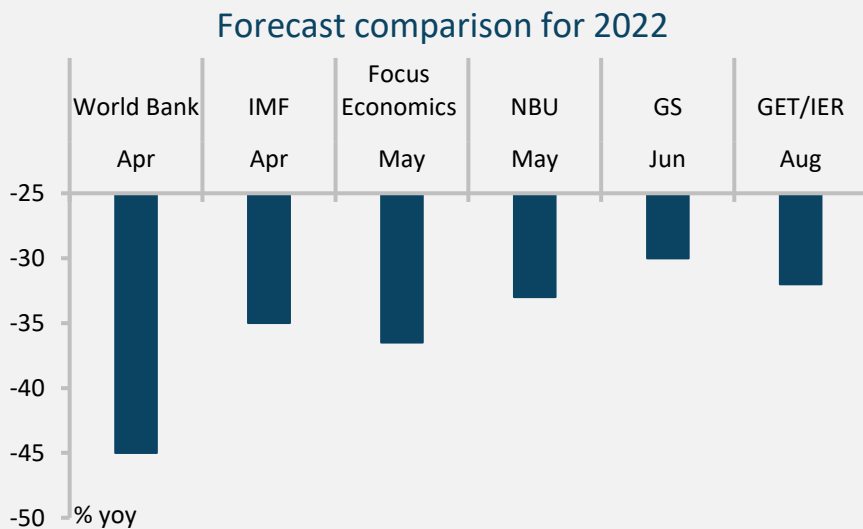


Source: Ukrstat, 2021; note: trade in goods

Economic growth



Sources: Ukrstat, GET/IER, *estimate



Sources: respective institutions

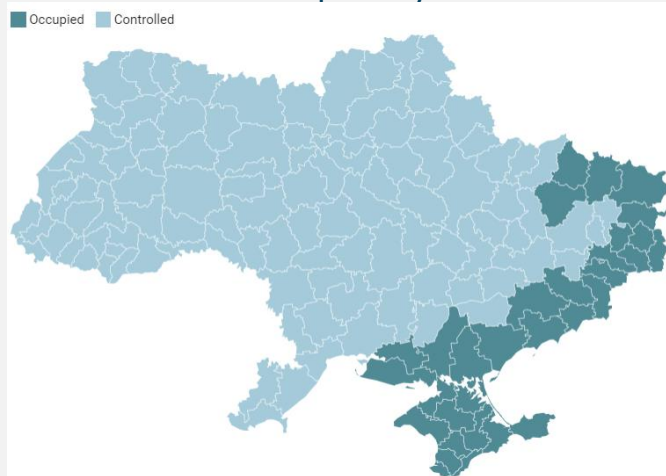
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- In 2021, Ukraine's economy grew by 3.4%, recovering from the COVID shock
- The war leads to a massive GDP decline of 32% yoy
 - Fighting/occupation ongoing in regions with approx. 20% of national GDP
 - Households lost incomes; migration
 - Destruction of capital stock and infrastructure
 - Destroyed/blocked ports account for >60% of goods exports

- **Uncertainty very high but recently signs of stabilisation**
- **Outlook, incl. for 2023, depends on the further duration and intensity of the war**

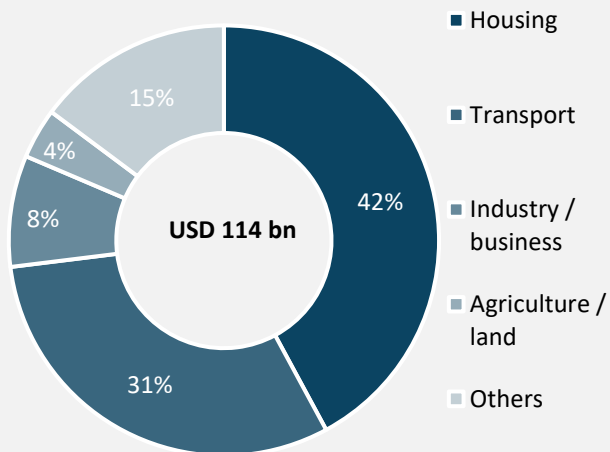
War damages

Territories occupied by Russia



Source: Own illustration, as of 26 August

Infrastructure damages



Source: Kyiv School of Economics, as of 22 August

Territories occupied and migration

- 20% of Ukraine's territory is occupied
- Approx. 6 m people are internally displaced and further 6 m left to other countries
- Unemployment rate at 35% in the 2Q

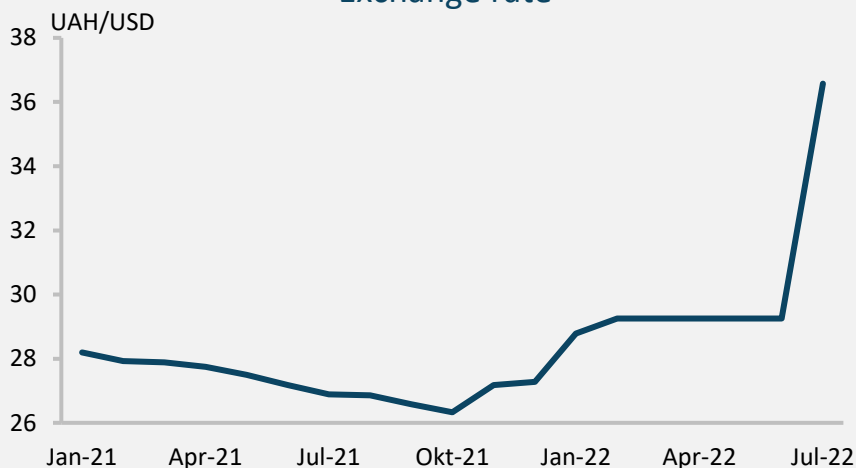
Infrastructure damage

- Damage estimated at USD 114 bn
- Large damage on housing (USD 48 bn) worsens perspective of people returning to their homes
- Transport damages (USD 35 bn) affect economic development

- **Massive destruction, steadily increasing**
- **Reconstruction process is of importance for Ukraine and its partners**

Exchange rate and current account

Exchange rate



Source: NBU

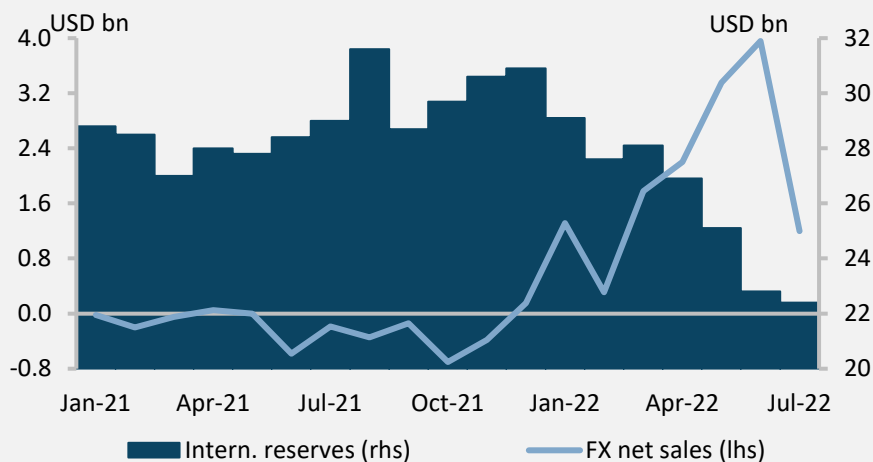
Exchange rate

- On 24-Feb, with martial law, the NBU fixed the exchange rate at UAH/USD 29.25 as a nominal anchor
- To maintain the rate, the NBU introduced capital controls

International reserves and FX interventions

- Interventions reached > USD 12 bn betw. Mar-Jul (43% of reserves in Jan-22)
- As reserves fell to USD 22.4 bn (-23% to Jan-22), the currency was devaluated to UAH/USD 36.57 in Jul-22

International reserves and FX interventions

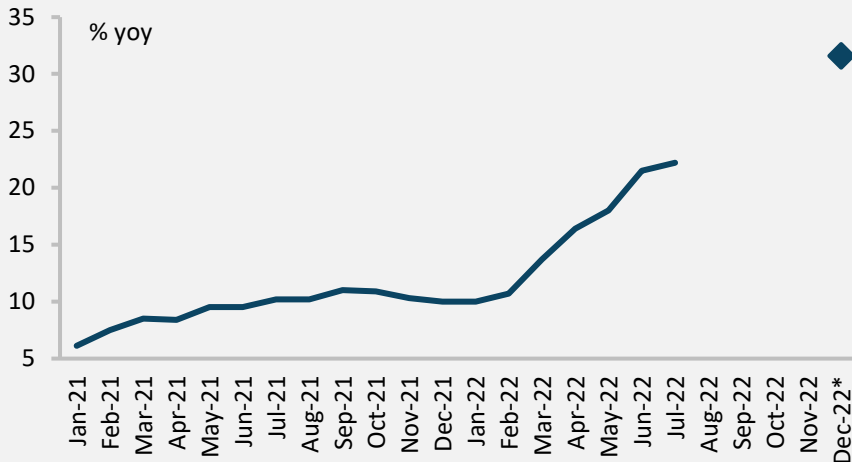


Source: NBU

- **Fixed exchange rate and capital controls will remain important for the duration of the war**

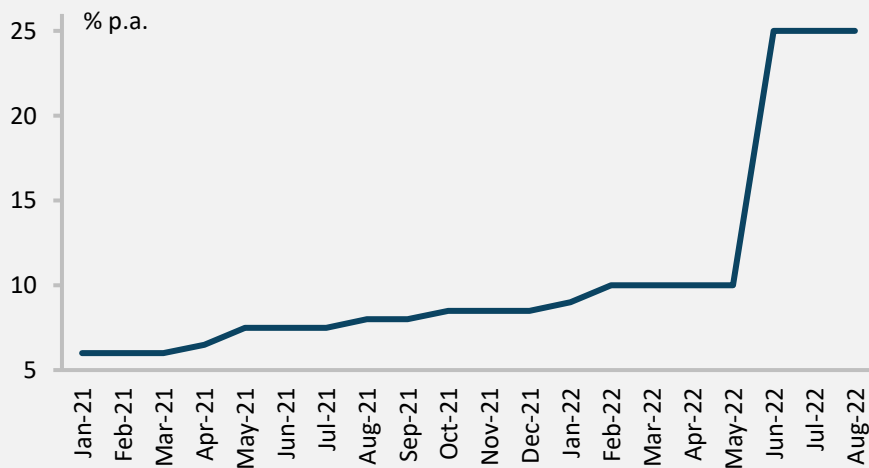
Inflation and monetary policy

Inflation rate



Sources: NBU, GET/IER, *GET/IER estimate for Dec-22

Policy rate



Source: NBU

Inflation

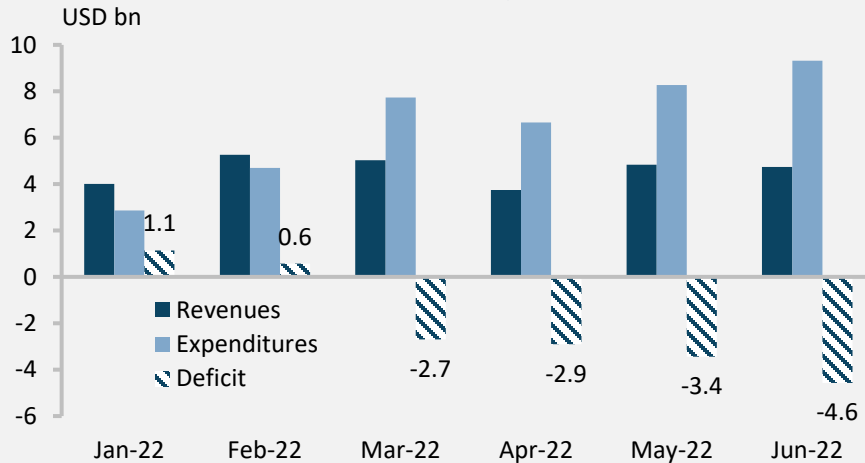
- The war also accelerated inflation
- NBU forced to rely on monetary financing with an inflationary effect, increasing pressure on the exchange rate
- Since Feb, monthly inflation approx. 3%, in July however 0.7%
- Overall, 22.2% yoy in Jul-22 and >30% expected for Dec-22

Policy rate

- Jun-22: hike to 25% p.a. primarily to stabilise the exchange rate
- **Temporary abandoning of inflation targeting as strategy during the war**
- **Monetary financing is an emergency instrument that should be limited**

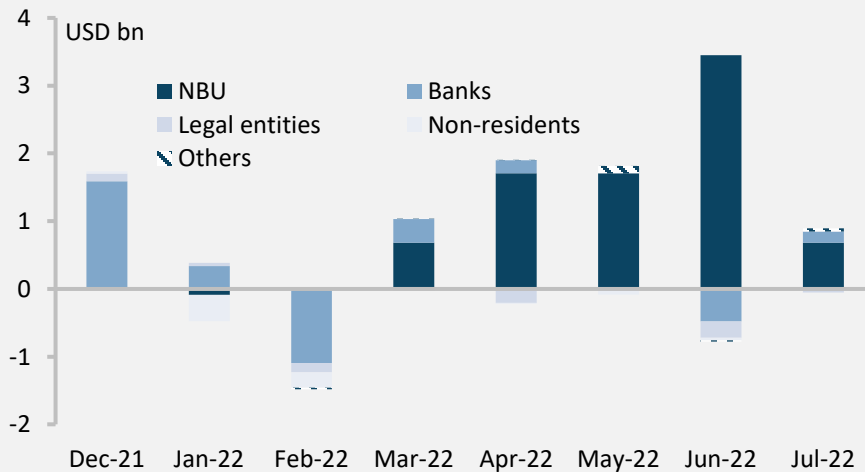
Public finances

Public budget



Source: NBU

Domestic government bond purchases



Source: NBU

Budget deficit

- War and economic decline negatively affect public finance on both sides:
 - Revenues decreased due to lower taxes
 - Strong expenditure increases, e.g. defence
 - Consequence: deficit in 2022 at USD 26 bn (18% of GDP), excl. grants USD 37 bn (26%)

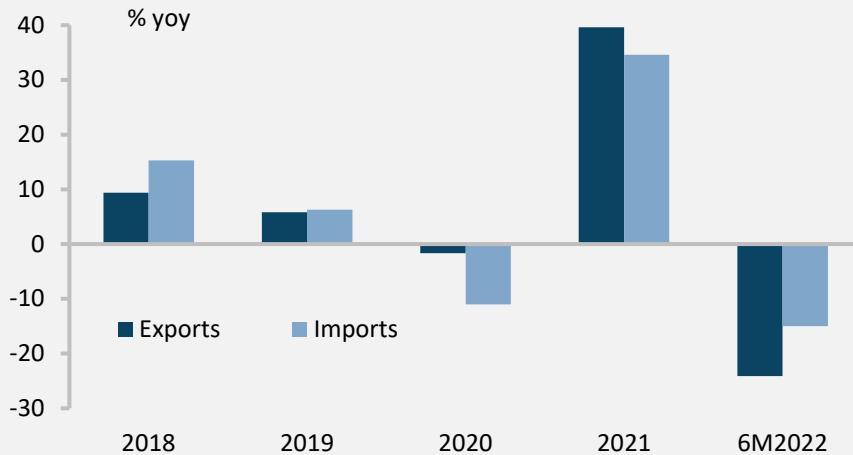
Financing

- Deficit mainly financed by the NBU with bond purchases >USD 8 bn, hardly any participation by private investors or banks
- Intern. partner play an increasingly important role
- Positive: debt suspension agreement with private investors and partner countries (USD 6 bn)

➤ **Public finance situation is critical, depends on international support**

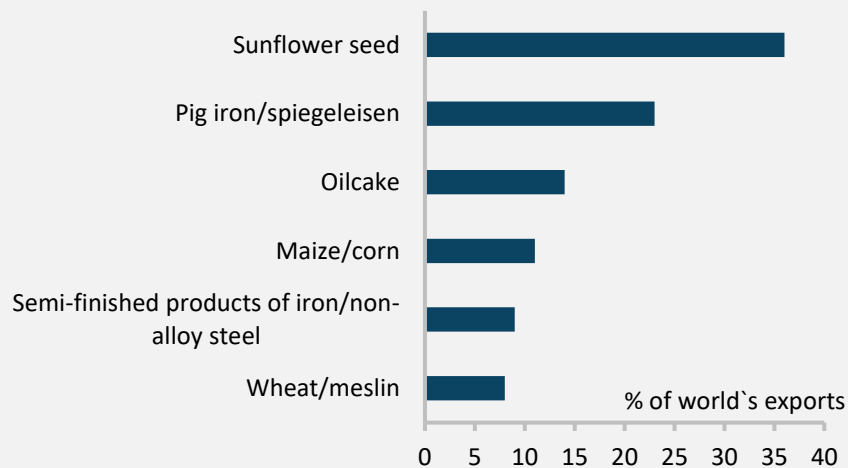
External trade

External trade in goods



Sources: Ukrstat, NBU, preliminary data for Jun-22

Important global export goods of Ukraine



Sources: World Bank, Trademap, 2021

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Exports and imports of goods

- Russia's blockage of ports since Feb-22 affect >40% of goods trade, particularly agri-food, metals, minerals
- 6M2022: these goods drive export decline (24% yoy)
- Imports fell less (-15% yoy) due to suspended import taxes (till 30-Jun)
- Decline driven by low machinery/chemicals imports as unblocked ports only cover agri-food

Global significance

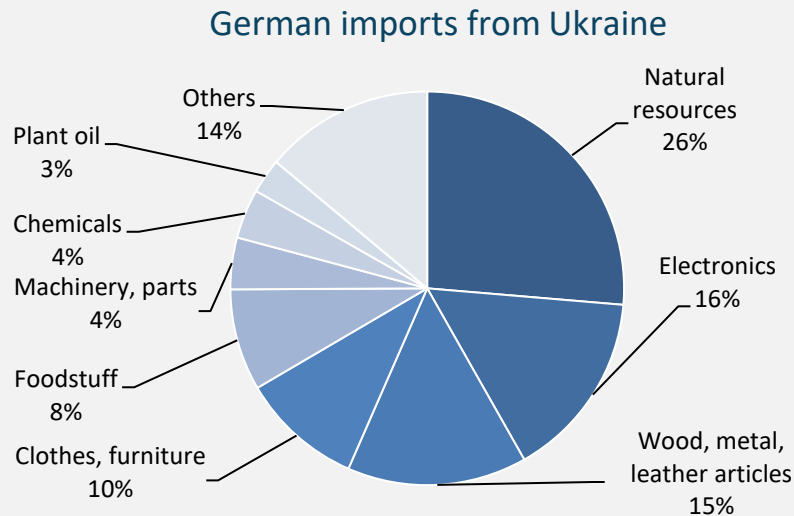
- Ukraine is one of the leading global agri-food and iron/steel exporters
- Gambia, Lebanon, Moldova, Djibuti each received >50% of wheat imports from Ukraine before war

- Exports massively declined due to port blockade/destruction
- Transport route diversification is important

Bilateral trade between Germany and Ukraine



Source: Federal Statistical Office; note: trade in goods



Source: Federal Statistical Office, 2021; note: trade in goods

Bilateral trade

- In 2021, the bilateral trade exceeded EUR 8.5 bn for the first time
- While bilateral trade developed positively until the war started, it has declined by 11% yoy in 6M2022

German exports to Ukraine

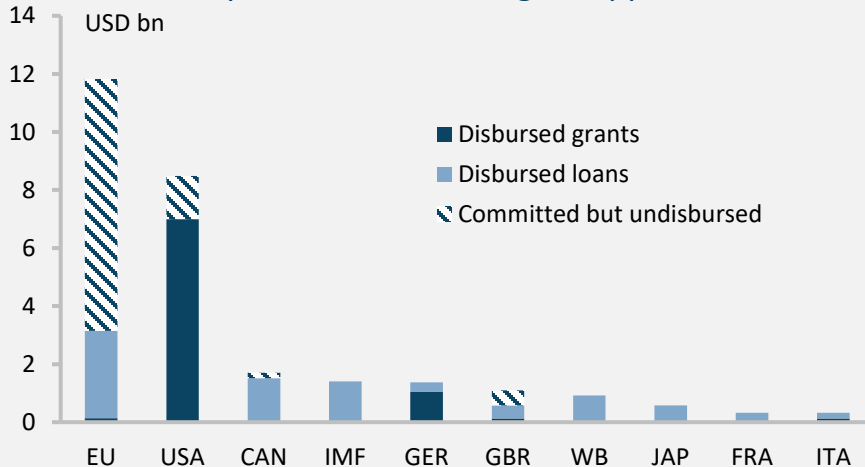
- Exports declined by 15% yoy in 6M2022, driven by reduced demand for machinery and parts

German imports from Ukraine

- Imports declined by 5% in 6M2022 as oil seeds and iron ore underlie export restrictions due to port blockade
- High prices for plant oil, metal products limit decline
- **Reduced economic activities in Ukraine and port blockage reduce bilateral trade**
- **But decline less sharp than for total trade**

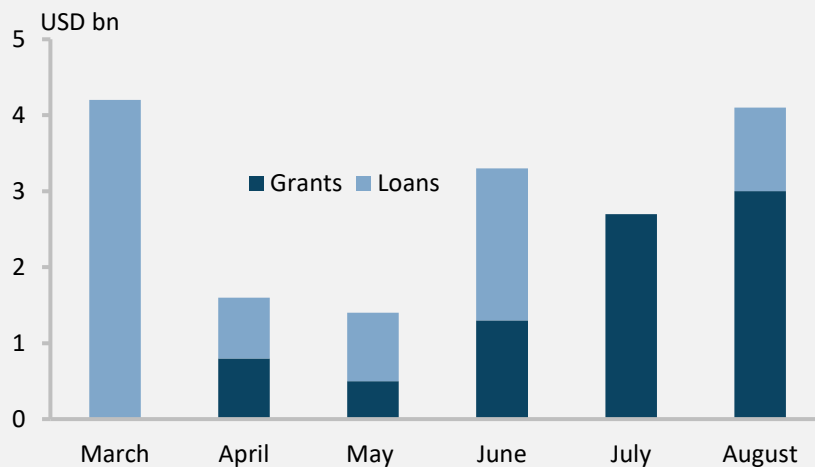
Financial aid

Top-10 donors of budget support



Source: Ministry of Finance, as of 23 August

Monthly distribution of financial aid



Source: Ministry of Finance, as of 23 August

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Budget support

- Ukraine/IMF forecast monthly fiscal need of USD 5 bn
- Partner countries announced budget support of approx. USD 31 bn (MoF) but only 55% was disbursed, more loans than grants

Form of support

- Support through (cheap) loans further increases debt burden, future debt sustainability problems possible
- Grants are therefore preferable
- Prospectively: consideration of using frozen Russian assets
- **Quick disbursements essential, grants over loans are preferred**

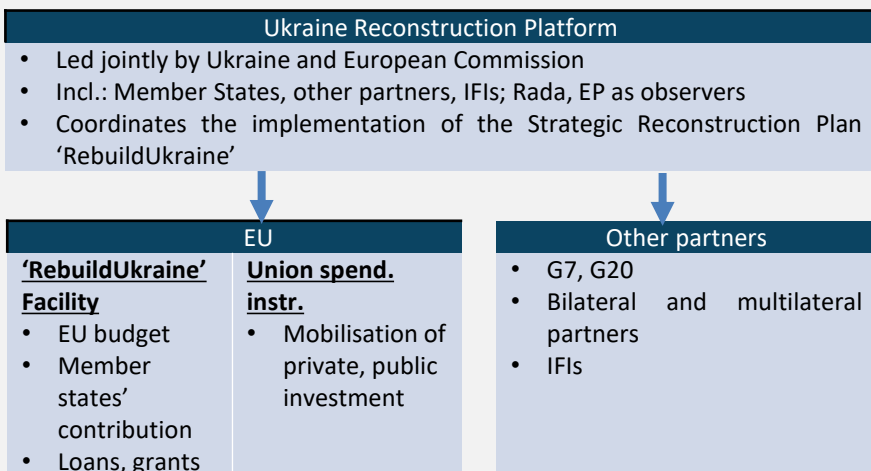
Reconstruction

Stages of reconstruction for Ukraine

Continuation of economy	Reconstruction of critical infrastr.	Revival of the economy	Transformation of institutions
Emergency support, special economic zones, minimise damage	Restore critical infrastructure, emergency housing	Restore econ. infrastr., return to macroec., fiscal stability	EU acquis, green, digital transformation
Stage 0: War time	Stage 1: 0 to 6 months after war	Stage 2: 3 to 24 months after war	Stage 3: Long-term perspective

Source: Becker et al. 2022, own illustration

Strategic reconstruction plan 'RebuildUkraine'



Source: European Commission, own illustration

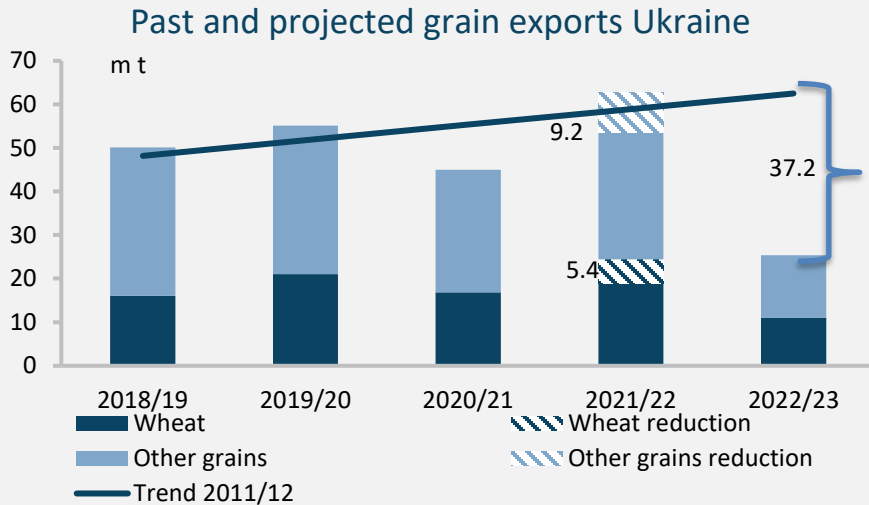
Stages of reconstruction

- Reconstruction will be a long process which needs preparation already as the war continues
- It requires domestic/international effort having a mind a long-term perspective

EU reconstruction plan for Ukraine

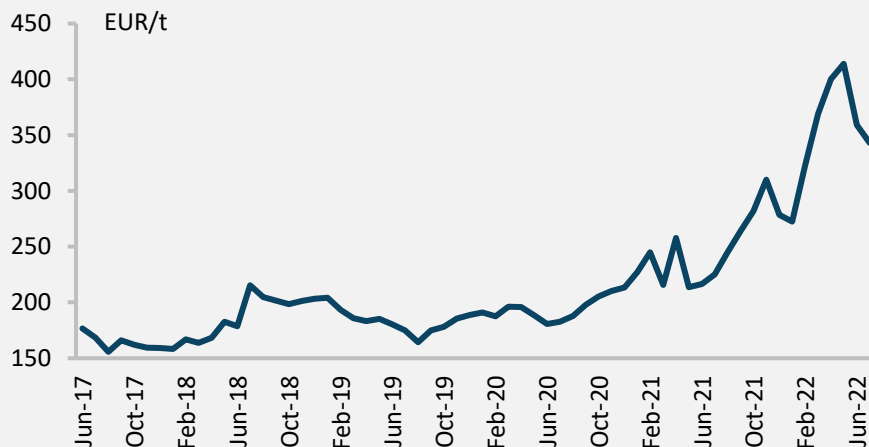
- EU proposal follows suggestions by international experts
 - Plan shall be owned by Ukraine, coordinated together with European Com. in the 'Ukraine Reconstruction Platform'
 - Joint coordination and monitoring body of financial sources
 - 'European Alliance of Cities and Regions for the Reconstruction of Ukraine' established to support on local level
- **Reconstruction effort requires the link between investment and reforms**

International food security



Sources: USDA WASDE Reports, own calculations

Monthly wheat prices on the MATIF futures exchange



Sources: Reuters, EURONEXT, end of the month

Grain exports

- Ukraine is among top-5 global exporters of sunflower seeds, maize/corn and wheat
- 2022/23 grain production estimated at 30 m t less than 2021/22
- 2021/22 15 m t less exports than pre-war forecast, 2022/23 37 m t below trend

Wheat prices

- Prices skyrocketed as demand is inelastic
- High prices are an existential threat to world's food insecure population, particularly in Africa and South East Asia
- **Damages to grain production and export transport infrastructure are tremendous and will take years to repair**
- **Port agreement is a positive step**
- **Exports hardly increased, high costs**
- **Ukraine's farmers hardly benefit from high world prices → 2023/24?**

About the German Economic Team



Financed by the Federal Ministry for Economic Affairs and Climate Action, 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.

**Advisory activities in Belarus are currently suspended.*

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