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**POLICY BRIEFING**  
**UKRAINE**

# Short-term estimation of Ukraine's public finance stance

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# Structure

1. Introduction
2. Macroeconomic background and assumptions
3. Estimation of the revenue side
4. Estimation of the expenditure side
5. Estimation of the fiscal gap
6. Financing the fiscal gap: recommendations and outlook

# 1. Introduction

## Motivation

- » Ukraine's war-torn economy seems to have reached its bottom during the summer of 2022, but real GDP is still projected to decline by 32% in 2022.
- » While budget revenues decreased due to the severe economic situation, expenditures have increased due to the military focus
- » Ukraine is currently cut off from foreign private borrowings, but funding needs are massive.

## Purpose of this Policy Briefing

- » Estimations of Ukraine's fiscal stance for the rest of the year.
- » Investigation of the fiscal and funding implications of the ongoing war for Ukraine's central government budget.
- » This Policy Briefing summarizes the results in the Policy Paper [07/2022](#).

## 2. Macroeconomic background and assumptions

### Macroeconomic background:

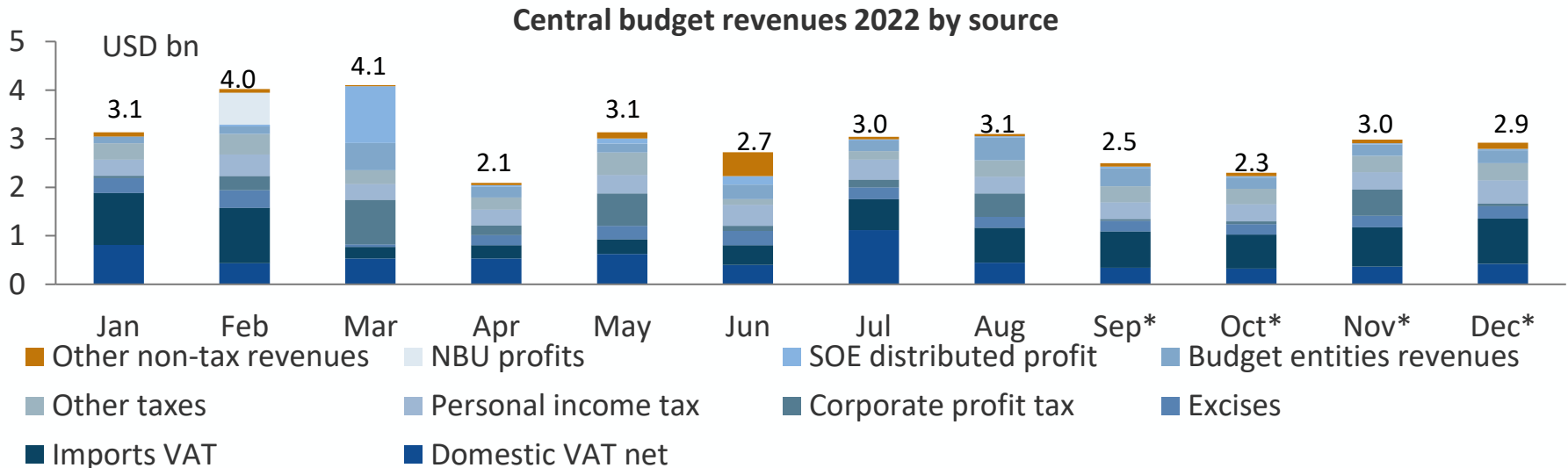
- » Real GDP is estimated to **decline by 32%** yoy for the total year and nominal GDP to fall to **USD 137 bn respectively UAH 4,433 bn**
- » **Inflation** will accelerate further to reach **31.6%** at the end of 2022
- » Loses due to the Russian aggression amount to at least USD 121 bn
- » **Unemployment rate of 35%** during the second quarter of 2022
- » **Exports fell by 28%** in the first seven months
- » **Imports fell by just 20%** in the first seven months

### Main assumptions:

- » A gradual **decline in active fighting** in the third and fourth quarter
- » **Sea ports remain blocked by Russia** not allowing for exports, except agricultural goods (“Istanbul Agreement”)
- » The **financial and banking sector** will remain **stable**
- » The government will keep **energy prices** for households **fixed** this winter
- » No further exchange rate adjustment is conducted (year average **UAH/USD 32.42**) and **capital controls remain in place** this year
- » No further key policy rate and tax policy **changes** this year

### 3. Estimation of the revenue side

- » The main growth driver for tax revenues is **VAT on import goods**, expected to increase significantly after the import VAT reinstatement in July.
- » Revenues are estimated using data on tax revenues from 2021, adjusted for the actuals of 1H2022, GDP and domestic consumption forecasts, projected Ukrainian hryvnia devaluation effects and consumer inflation



Sources: NBU, MoF, Parliament, GET/CES estimates for September-December

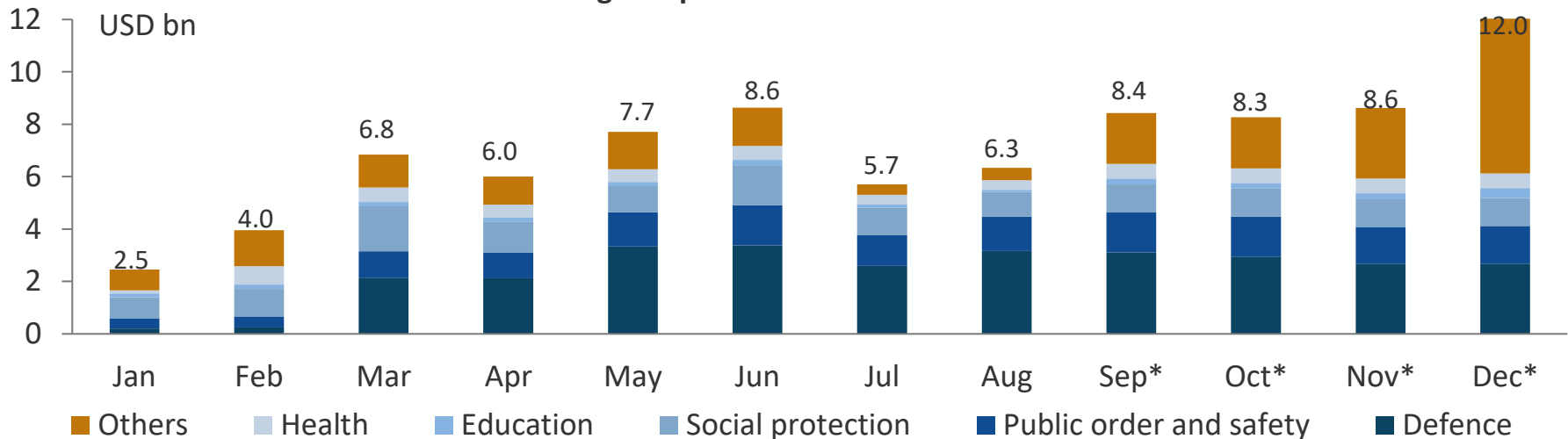
- The state budget will be collecting USD 10.3 bn in Sep-Dec from tax and non-tax sources.
- **Total revenues of USD 36.0 bn in 2022.**

## 4. Estimation of the expenditure side (1/2)

### Scenario 1: Based on the current Law on the State budget

- » Expenditures in the budget law are used as the baseline, adjusted for the elevated military and public order expenditure.
- » While most other expenditures were severely restricted, the focus in military expenditure from 7% in Aug-21 to 46% in Aug-22 brought the total budget expenditures to increase significantly

Central budget expenditures 2022 under scenario 1



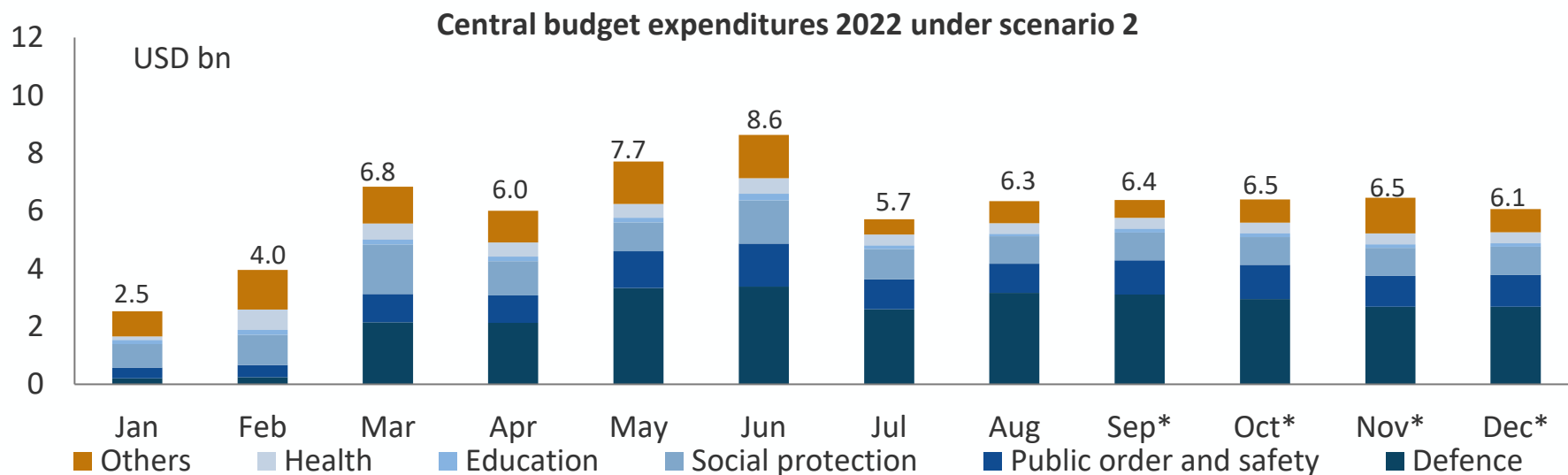
Sources: NBU, MoF, Parliament, GET/CES estimates for September-December

- The estimation shows that Ukraine will have to spend approx. **USD 8.4 bn** on average **monthly** during Sep-Dec.
- December is an exception: traditional end-year expenditures peak elevates expenditure to USD 12 bn.
- **Total annual expenditure of USD 85 bn in 2022.**

## 4. Estimation of the expenditure side (2/2)

### Scenario 2: Integration of possible expenditure cuts

- » Budget savings are crucial in this scenario due to inadequate foreign financial aid.
- » Expenditures will be kept at an average of the May-August level for all the categories, except for debt servicing and military and public order expenditures, for which the assumptions of the previous scenario hold.
- » This scenario is much more probable.

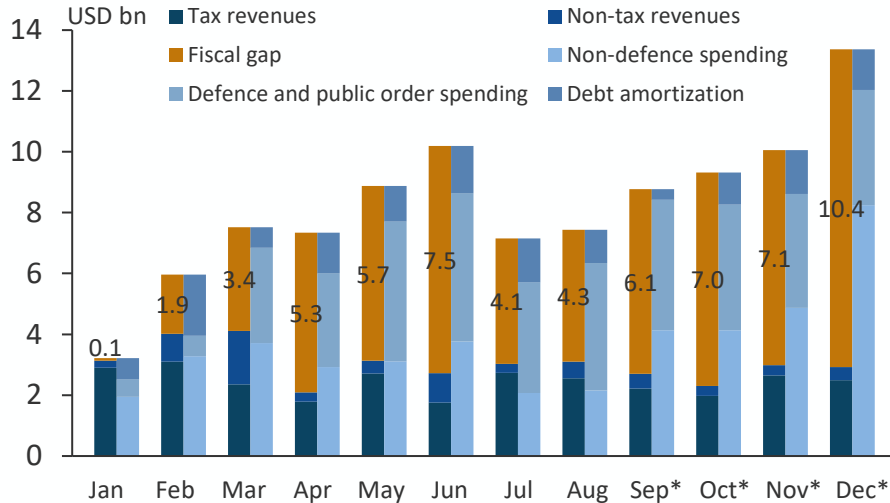


Sources: NBU, MoF, Parliament, GET/CES estimates for September-December

- Average spending of **USD 6.3 bn per month** through Sep-Dec.
- Further expenditure cuts are difficult and unlikely.
- **Total annual expenditure of USD 73 bn in 2022**

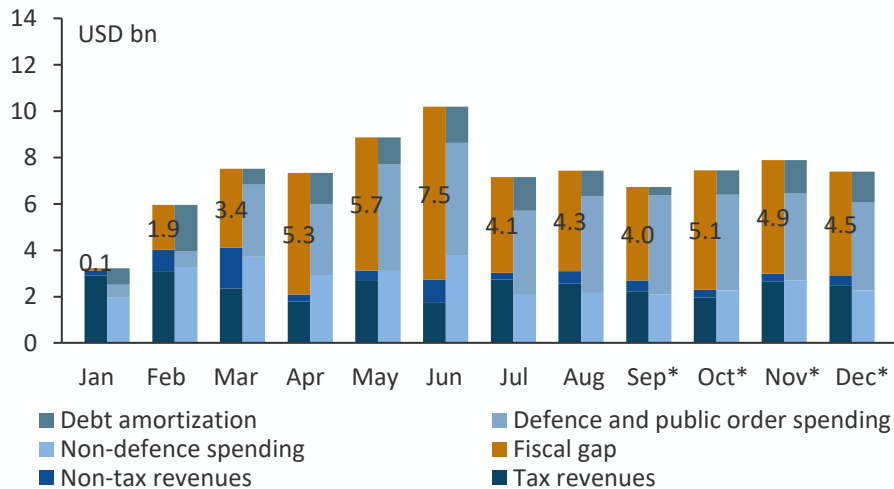
## 5. Estimation of the fiscal gap (1/2)

### Government revenues and expenditures under scenario 1



Sources: NBU, MoF, Parliament, GET/CES estimates for September-December

### Government revenues and expenditures under scenario 2



Sources: NBU, MoF, Parliament, GET/CES estimates for September-December

### Scenario 1:

- » We estimate the Ukrainian budget deficit to amount to **USD 49.0 bn** in 2022 (35.8% of GDP)
- » Taking debt amortization into account, the **fiscal gap** amounts to **USD 63.1 bn** (46.1% of GDP)

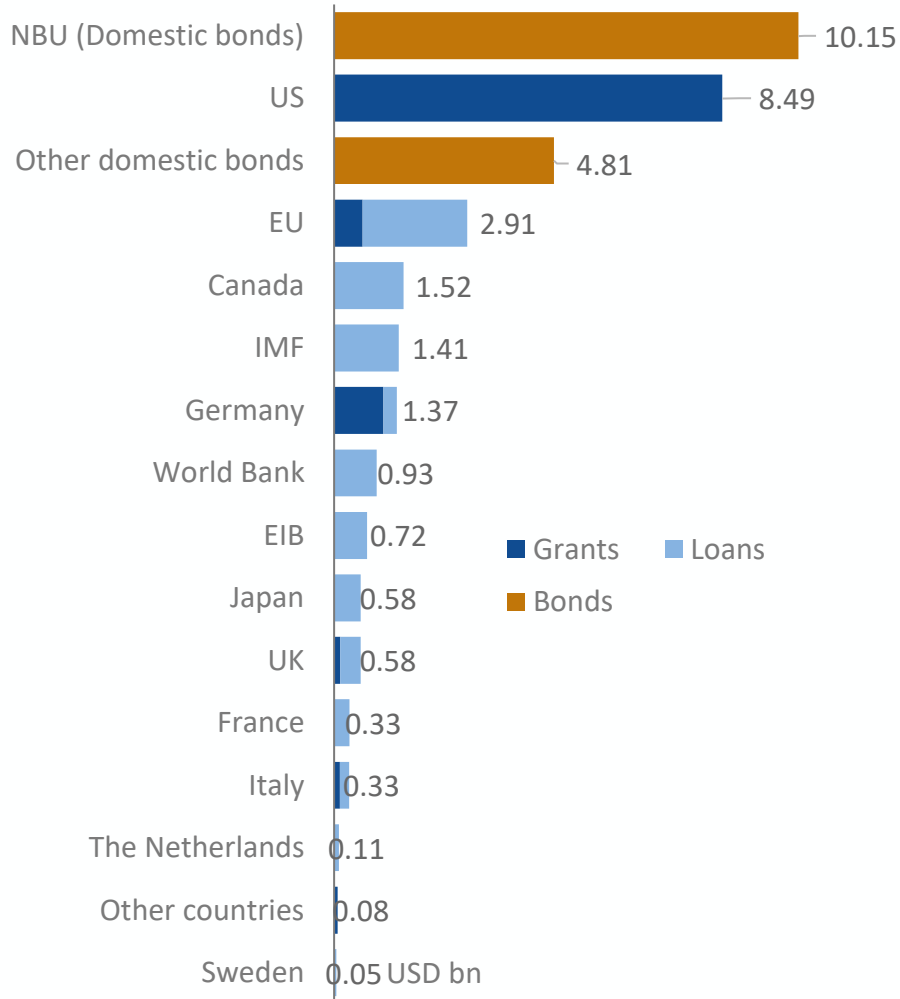
### Scenario 2:

- » The savings budget scenario (scenario 2) would translate into a **USD 37.0 bn** deficit in 2022 (27.1% of GDP)
- » Taking debt amortization into account, the **fiscal gap** amounts to **USD 51.1 bn** (37.4% of GDP)



## 5. Estimation of the fiscal gap (2/2)

### Ukraine's state budget financing 24 February



Source: Ministry of Finance of Ukraine as of 28 September 2022

### Financing of the gap in different scenarios

- » Bond purchases account for USD 15 bn
- » International partners disbursed USD 20 bn from committed USD 36 bn

#### Scenario 1:

- » Estimated gap: USD 63 bn
- » Assuming full disbursements of committed aid already this year
- **Financial needs of USD 12 bn remain**

#### Scenario 2:

- » Estimated gap: USD 51 bn
- » Assuming full disbursements of committed aid already this year
- **The gap will be covered**

## 6. Financing the fiscal gap: recommendations and outlook

- » The estimated fiscal gap is between 51.1 bn and USD 63.1 bn (37.4% and 46.1% of GDP, respectively) in 2022, depending on the modelled scenario.
  - » Private external capital markets are not available; the local debt market is rather small; debt monetization should be curtailed because of its macro-financial risks.
  - » Bilateral and multilateral financial assistance come in as the last resort.
  - » Scenario 1: We see that the overall pledged and secured amount of financing is not enough in the case of scenario 1 – **with a USD 12.0 bn gap**
  - » Scenario 2: **But is roughly equal** to our gap estimation.
- 
- **Disbursement of foreign assistance must be sped up;**
  - **Grants should dominate the assistance structure over loans; predictability of disbursements is important**
  - **Close coordination of financial aid between partner organisations/countries is needed**
  - **Comprehensive and substantial financial and military support to Ukraine will help to win the war more quickly instead of dragging it out into a prolonged one.**

# 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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