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HOW THE WORLD ENTERS 2023: ECONOMIC PROSPECTS FOR UKRAINE'S RECOVERY

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HOW THE WORLD ENTERS 2023 ECONOMIC PROSPECTS FOR UKRAINE'S RECOVERY

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Although the war in Ukraine still ravages and no one knows when it ends, there are reasons to expect the Ukrainian army's gradual victory, therefore it is already vital for Ukraine to form a vision of the country's development and ways for finding responsible and effective directions to shape a restored (new quality) state.

Conditions for the development of Ukraine's economy in 2023 will be determined by a complex combination of multidirectional internal and external factors, which will be further intensified by international confrontations between world political and economic leaders, as well as by the high risks of continued full-scale Russian aggression. We do not ignore such risks, but despite them, we see rational opportunities for stabilising Ukraine's macro-economic environment.

At the same time, the nature of fighting in early 2023 suggests cautious optimism about the coming year. Although the risks of continued full-scale Russian aggression remain high, the reasons for such optimism are as follows:

- ✓ we believe that the Armed Forces of Ukraine will gradually drive the aggressor out of the country, liberating the territory for economic and humanitarian recovery;
- ✓ although countering the aggression requires significant human and financial resources, proper security of the country, including with the help of partner countries, will become the basis for peaceful construction of the renewed country.

Speaking of Ukraine's economic problems over the past decades, the answer seems to be clear – it is the limited ability of the country's political leadership of almost any party affiliation to consistently implement decisions in the interests of the country and excessive concern for its own political and economic benefits. Today, as the victory approaches, there are examples of resumed politicisation of the economy and economic policy. The demonstration of non-transparent work patterns in making and implementing political decisions by the government leads to imbalance, including further escape to shadow, of relations in the economic and social spheres across the country.

Meanwhile, the fact that the Ukrainian economy demonstrates impressive signs of resilience in the face of lasting large-scale Russian aggression, conveys positive signals that the lessons of previous crises will be taken into account and duly considered by the government in the country's recovery. It is during this period that the country will face significant challenges and risks. If the country has demonstrated examples of solidarity to repel aggression of «understandable» enemy, then, unfortunately, this does not guarantee that the unity of action will be maintained in the future. The history of Ukraine shows that the greatest losses of independence and freedom occurred in times of peace, when patriotic forces failed to consolidate and lost people's trust while in discord, thus «providing» anti-Ukrainian forces with the conditions for revenge.

Today, however, one can expect the country's successful peaceful recovery, including

thanks to partner countries. Ukraine, which consistently fits into the geo-economic space, is increasingly affected by the processes in the world economy, which are formed largely under the influence of the world's largest economies.

As the coronavirus crisis somewhat subsided, 2022 was seen as a peaceful and economically successful year for humanity. The post-COVID recovery of global economic activity in the autumn of 2021 was significantly slowed down by the devastating full-scale war in Ukraine. Moreover, Russian aggression has provoked a «perfect storm» in both security and economic spheres, even for economically strong members of the EU. Energy blackmail of Europe and grain blackmail of emerging economies has eloquently revealed the fragility of the modern world order, its weakness in the face of provocative negative intentions and actions.

Key economic impacts associated with the war in Ukraine include global inflation, which has become one of the most important factors in slowing down the world economy in 2022, also affecting the leading global economies. From the very beginning of inflation's shock unwinding, it became clear that it was part of Russia's hybrid war against the democratic countries in Europe, which, of course, would have significant macroeconomic effects in the medium term. *On the one hand*, it will weaken growth incentives for the real sector, and will affect the value of national currencies, foreign trade and investment flows and debt positions *on the other*. And it must be admitted that this has indeed happened in most countries.

In general, one can assert that the current economic troubles in most countries are caused by the accumulated negatives and their effects – the Global Financial Crisis of 2008-2009 and the global coronavirus shock of 2020-2021 – and related restrictions on trade and movement of people, the destruction of global value chains. It continued with this year's high inflationary pressures provoked by Russia in the energy and food markets, tightening monetary policies of major central banks and the ensuing global strengthening of the dollar, which leads to higher production costs, and thus to a decrease in demand in leading economies and economic slowdown in general.

These are external challenges that are shaping the processes of Ukraine's recovery. It should be admitted that so far, people's assessments of economic situation in the country are rather low. However, they do not suggest economic collapse. Moreover, since the domestic economy managed to preserve a significant share of its potential in 2022, this gives grounds to believe that 2023 can truly be the year of economy's gradual recovery. And society fully supports the government in the fight against Russian aggression. It is safe to say that this is a significant component of the Ukrainian Armed Forces' military victories.

However, in matters of post-war peaceful construction, the authorities' decisions and actions are already causing increasing concern. Therefore, transparency and meaningfulness of government decisions is a prerequisite for accelerated recovery of the country, even in the face of enemy attacks.

As for our vision of the country's immediate economic prospects, it should be borne in mind that the downfall of the economy caused by Russian aggression in 2022 has formed a very **low comparison base** for the following years. Therefore, possible positive growth indicators in 2023 should adequately take this factor into account.

Whatever the progress, however, it is not yet a question of Ukraine entering the path of stable and balanced development. Rather, it is about «licking wounds», rebuilding and restoring housing and critical infrastructure, which will create minimally acceptable living conditions across the liberated territory of the country.

According to our expert observations, we tend to estimate Ukraine's economic growth in 2023 somewhat higher than the government's vision – **real GDP growth at 4-4.5%**. In addition to economic incentives, this will have a high social and psychological stimulus, improving the quality of households' well-being, which, in turn, will strengthen the stabilisation and recovery processes.

Favourable factors include the following:

- ✓ reinforcement of the Armed Forces of Ukraine, which will accelerate the liberation of the country, free new territories, and boost the ability to protect

the country from enemy bombing and other sabotage attacks;

- ✓ continued provision of military and financial aid by developed partner countries, which will strengthen Ukraine's defence capabilities, replenish foreign exchange reserves and protect the hryvnia from devaluation shock, thereby forming the basis for sustainable recovery;
- ✓ launch and implementation of international programmes and projects to rebuild Ukraine's economy (the so-called Marshall Plan) despite the enemy's continued aggression, primarily through the restoration of physical infrastructure;
- ✓ improvement of the population's well-being, its better adaptability to enemy attacks, and increased optimistic expectations, which will be an additional factor and stimulant of production gains;
- ✓ return of Ukrainians who were forced to leave the country earlier, their readiness to be involved in production processes;
- ✓ improvement of mutual understanding between the US and EU with China, which will reduce the risks of economic and security imbalances and will also help expand Ukraine's economic cooperation with China, which does not harm Ukraine's strategic interests and does not threaten its strategic partnership with the United States;
- ✓ inhibition of energy complications in Europe and restoration of aggregate demand, primarily in the partner countries of the CEE region, which will strengthen the export capacity of the domestic economy;
- ✓ increased cooperation between the National Bank of Ukraine and the government aimed at supporting the real sector.

On the other hand, **inhibiting factors** include:

- ✓ slow pace of recovery of the global economy in general, and of the leading economies in particular, which, as noted, largely determine the formation of

global demand, primarily due to tighter monetary policy and high interest rates to counteract high inflation;

- ✓ IFIs' unpreparedness to consistently support Ukraine, untimely provision of agreed financial resources to the country, delayed allocation of funds for political considerations (Ukraine's poor completion of «homework»);
- ✓ intensification of crisis processes in China, which may negatively affect global trade flows and increase the risks of China's strategic cooperation with Russia;
- ✓ Russia's access to the bomb systems of other countries that are unfriendly to Ukraine, which will increase the destruction and human losses;
- ✓ aggravated confrontation and contradictions between the state's fiscal approaches aimed at expanding the tax base and the interests of business development and stimulation.

Given the sensitivity of Ukrainians to exchange rate dynamics, a rational currency policy should become an important stabilising factor in the entire economic environment, where a weak devaluation of the hryvnia will be acceptable (and in some aspects, even desirable), reducing the risks of reserve leaching and capital flight, and helping balance the supply and demand for currency in the cash markets, without letting the hryvnia float.

The «grain deal» and the formation of grain hubs on Ukraine's western borders will stabilise Ukrainian agricultural and food exports, which will help determine the supply of such goods on domestic markets and have a steadying effect on domestic consumer markets, thus preventing an inflationary shock in 2023. Under these conditions, although consumer prices will continue to rise gradually, the (estimated) inflation rate will not exceed 20%, that is, it will be lower than in 2022.

If international programmes for Ukraine's recovery are launched starting in the second half of the year, then one can expect contradictory effects in 2023. *First*, a significant increase in imports of goods and services to

be used to meet consumer and project needs will result in the growing foreign trade deficit, which will put pressure on the exchange rate. *Second*, the inflow of (investment) capital as part of the Marshall Plan projects will intensify, financing part of Ukraine's trade deficit. At the same time, significant resources to help Ukraine will continue to come from partner countries, and this will fully cover the emerging deficit and help strengthen the hryvnia.

Leading countries and international financial institutions will obviously continue their financial support for Ukraine in 2023. In this context, it is important to know which shares of the resources provided will be in the form of grants and loans, respectfully. Grant assistance would clearly be more appropriate, by not worsening the country's debt position. However, not all potential sponsors are ready to take such steps. Therefore, given external payments, there are reasons to expect a slight increase in total external debt and public debt. At the same time, the debt in GDP terms

is likely to decline, as the dollar equivalent of GDP will increase in 2023 amidst mild devaluation.

We are fully aware of the risks of the post-war recovery. If the country has demonstrated examples of unity to repel aggression of «understandable» enemy, then this does not mean that the strong unity of action will continue in the future. The history of Ukraine shows that the greatest losses of independence and freedom occurred in times of peace, when patriotic forces failed to consolidate and lost people's trust while in discord, thus «providing» anti-Ukrainian forces with the conditions for revenge.

Meanwhile, we emphasise once again that Ukraine has sufficient potential to improve its socio-economic dynamics. And today, there are reasons to expect that the country's peaceful restoration will be successful, including thanks to partner countries. And rational institutional changes will allow this potential to be fully realised.