BOFIT blog

Ukraine's economy grows amidst the rising toll of war

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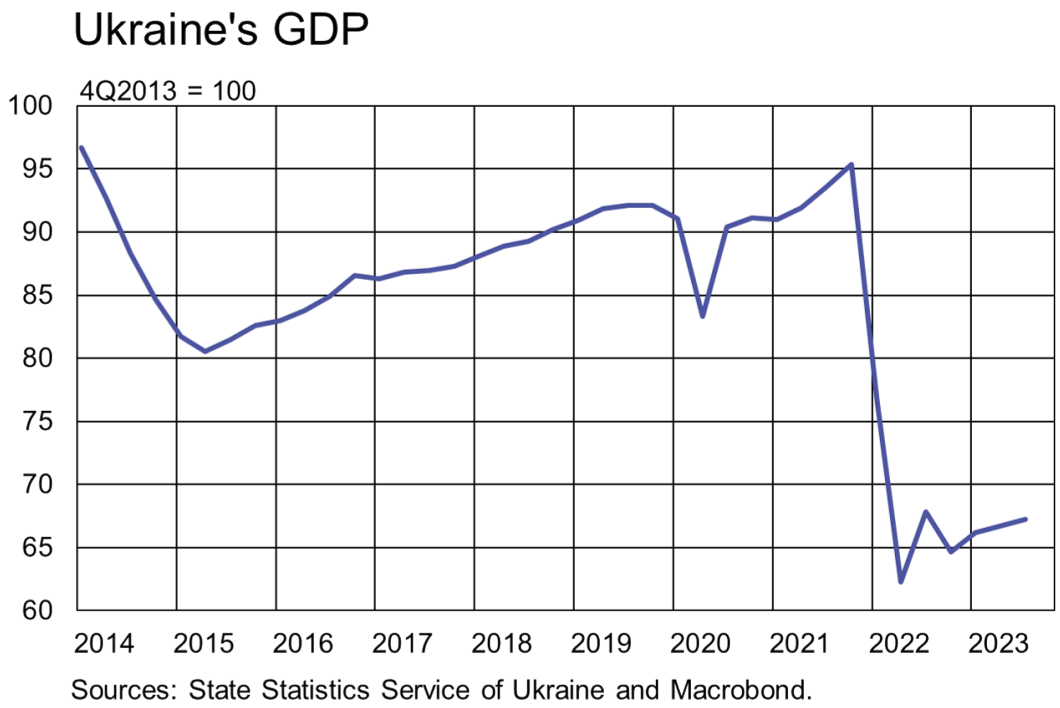
This Saturday marks the second anniversary of Russia's unprovoked invasion of Ukraine. We should remember, however, that Russia's war on Ukraine began a decade ago following the Maidan protests. The illegal annexation of Crimea and territory in and around four regions, along with sham elections and treatment of Ukraine as a fiction, highlight the incessant nature of Russian abuse.

Ukraine has made huge sacrifices to repel Russian aggression. Thousands of civilians have died and tens of thousands injured since the February 24, 2022 invasion. Millions of Ukrainians have been forced to evacuate their homes and move at least temporarily abroad or elsewhere in the country. Along with the human suffering and displacement, war has scarred Ukraine's economy. GDP contracted by about 29 % in 2022, which is understandable as war prevents or interferes with many economic activities. These negative effects, however, were exacerbated by the fact that a significant share of Ukraine's export industries (and most of its infrastructure serving foreign trade) is located in the southeastern and southern parts of the country. Significant shares of production facilities, transport hubs and energy infrastructure have either been demolished or occupied by Russian forces.

The government deficit, which reached around 16 % of GDP by the end of 2022, was almost exclusively financed by the National Bank of Ukraine in the early months of the war. Fortunately, Ukraine's partners in Europe and elsewhere – together with support from international

institutions promoting stability of the global financial system (IMF, World Bank, EBRD) – stepped up in the latter half of 2022 to help fund the huge gap in Ukraine's public sector finances.

Chart 1.



With the frontlines stabilizing and improving air defences of cities, economic activity began to revive. This was particularly true in the western parts of the country, bolstered by the influx of displaced people (which meant, of course, that labour capacity was lost in eastern and southern areas). Ukraine's economy returned to positive growth in late 2022, and recovery of continued last year. 2023 GDP growth is now estimated at about 5 % (and perhaps slightly more). Stabilization of the conflict in the east and south also fuelled domestic demand as many who had fled the country at the start of the war could return. The output of industries that support the war effort also increased significantly, and access to international financing eased. Ukraine managed to push the Russian navy away from its territorial waters, making it possible to raise the volume of grain shipped via the Black Sea close to pre-invasion levels. Besides critical Black Sea shipping, Ukraine also developed alternative grain shipping routes to world markets such as the Danube. Functioning land borders with the European Union are today essential for Ukraine's economy.

Ukraine's growth is expected to continue. In December, the IMF forecast that Ukraine's GDP will grow by 3.2 % this year. In January 2024, the research firm Consensus Economics reported that its average of major forecasts for 2024 see Ukraine's GDP rising by 4.3 % this year and 5.4 % next

year. While forecasts are naturally subject to uncertainty from changes in the course of the war, last year's favourable trends allow for cautious optimism. The economy could even recover quite briskly with a cessation of hostilities.

Nevertheless, as long as most of Ukraine's infrastructure and productive capacity remains damaged, destroyed or in Russian hands, only a partial recovery is possible. A recent joint survey by the World Bank, UN, European Commission and Ukraine determined put the cost of repairing war current damage in Ukraine at 486 billion dollars, or nearly triple Ukraine's 2023 GDP. The EU this month reached agreement on a financial assistance package of 50 billion euros over the period 2024–2027. While the assurance of stable financing is essential to Ukraine, the acute need remains for financial resources to repair war's havoc.

Ukrainian society today cannot function without a constant effort to repair damage inflicted by Russia, but its full recovery requires peace. This is why Ukraine deserves all possible assistance right now to finish the war.

Keywords

reconstruction, Ukraine, war