CENTRE FOR ECONOMIC STRATEGY

UKRAINIAN ECONOMY IN WAR TIMES

RAPID ASSESSMENT, APRIL 2022

DATE: April 11, 2022

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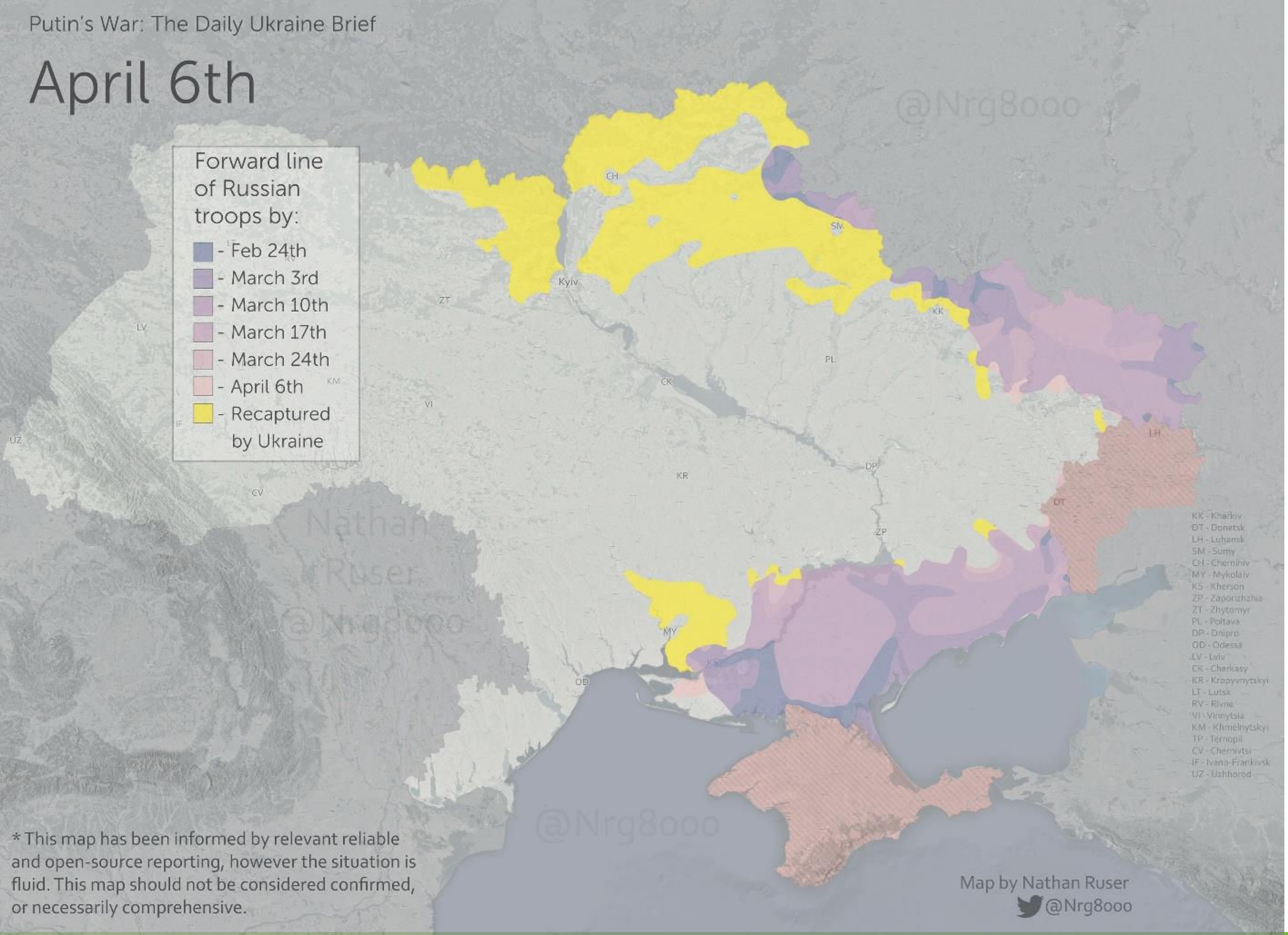

- General economic consequences
- Physical damages assessment
- Migration and human capital
- Policy response
- Fiscal gap
- Policies outline for the future

GENERAL ECONOMIC CONSEQUENCES

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Devastating effects on every side of economic life

- GDP forecasts from -10% (IMF) to -45% (WB), electricity consumption drop by ~35% in March.
- Over half of the business activity frozen (57% according to EBA, 59% according to KSE)
- Exports at 50% of pre-war volumes, imports at 30% of pre-war volumes with a heavy ban on imports and collapse of the exports logistics
- Maritime logistics (62% of exports in 2021) effectively blockaded by Russians

GENERAL ECONOMIC CONSEQUENCES

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Devastating effects on every side of economic life

- Consumer prices rose 4.5% in March compared to February, the annual figure very likely to exceed 15%
- Banking sector reportedly lost 50-70% of cash flow from loan portfolio, NPL and capital adequacy problems mounting, but the system is up and running
- Currency depreciation was negligible, but it took the severe capital controls to hold the currency crisis at bay
- Investments are frozen and unlikely to widely rebound without special war risk insurance policies

PHYSICAL DAMAGES ASSESSMENT

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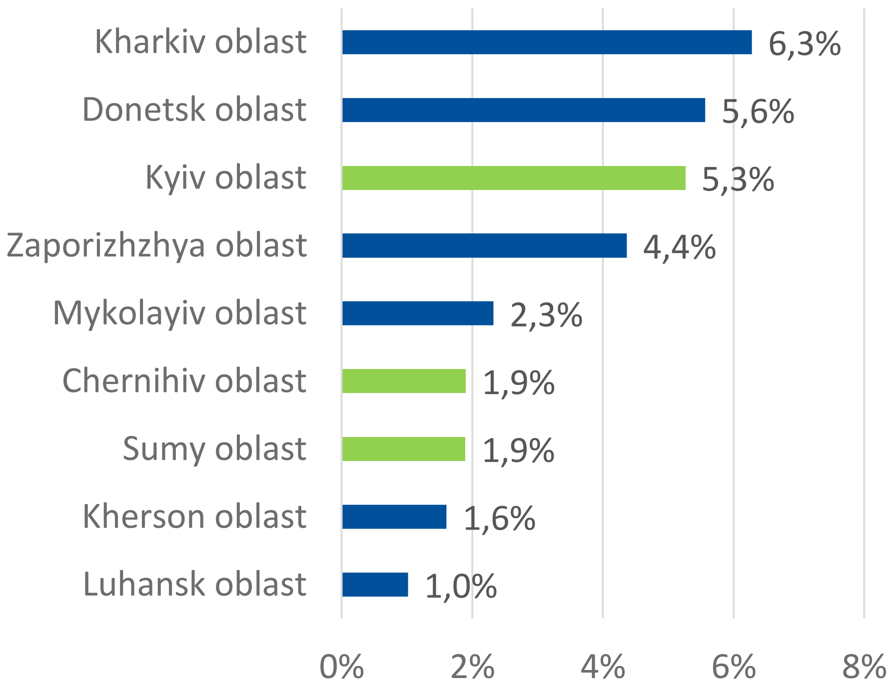
Over $80 bln and counting, regions with 30% of the national GDP affected…

TOP-5 damaged industrial assets

Asset	Location	Industry	Assets, $ mln*
MMK Illicha	Mariupol (Donetsk oblast)	Base metals	1 893
Azovstal	Mariupol (Donetsk oblast)	Base metals	1 444
Ukrainian energy machines	Kharkiv	Heavy industry	417
Antonov	Kyiv	Aircraft building	385
Kremenchug oil refinery †	Kremenchug (Poltava oblast)	Oil refinery	374

Share of affected regions in GDP



PHYSICAL DAMAGES ASSESSMENT

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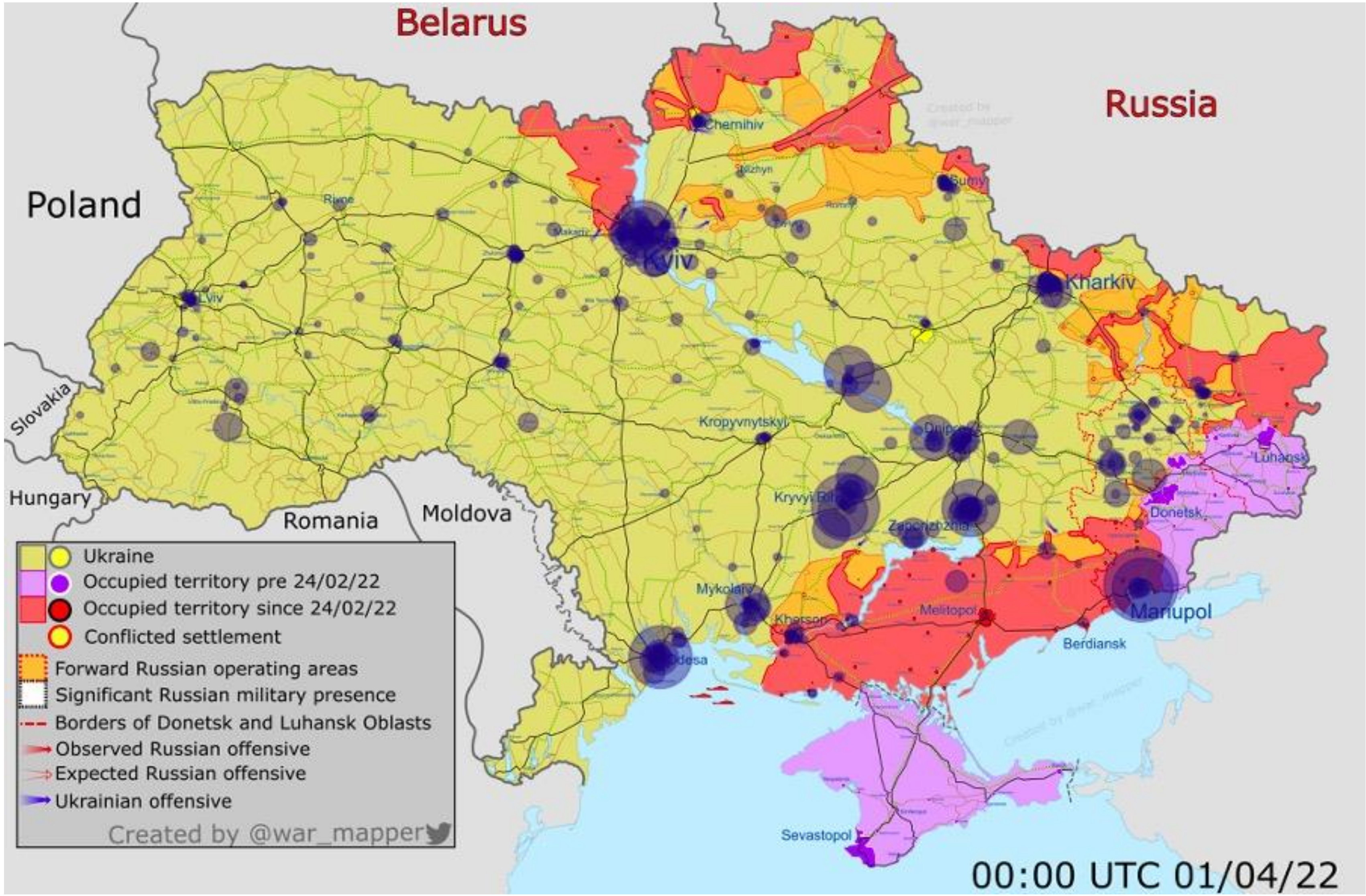
…and more at risk



HUMAN CAPITAL AFFECTED BRUTALLY

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4.2 mln fled the country, 6 mln more are displaced, half of them might never return

POLICY RESPONSE

Timely, radical, limited by the lack of resources…

Taxation and business support

- The turnover limits for simplified taxation system eligibility were lifted. Now every enterprise can choose to pay 2% sales tax or remain on the general taxation system with VAT and corporate profit tax.

  VAT-free imports for entities on STS were introduced.
- Customs duties and excises were cancelled for all goods (except those from Russia, Belarus and temporarily occupied territories).
- Fuel VAT was declined to 7%, local transportation services VAT declined to 7%.
- Labor code temporarily simplified, easing the burden on employers

POLICY RESPONSE

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Monetary and currency regulations

- The government acted upon prices growth with VAT decline and regulating prices for several types of critical goods and services
- The NBU provided refinance to support banking system liquidity and keep it up and running
- Capital and current account controls were severe and imposed immediately: imports ban, FX rate fixed, capital outflow restricted
- The banks will have time to figure out their recovery strategies as the prudential regulations were waived on NPL and capital.

FISCAL GAP

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... because there're far not enough resources to cope with a crisis of such scale

The deficit reached $3 bn in March…

	January	February	March
General fund revenue, $ bn	2.8	3.7	3.5
General fund expenditures, $ bn	2.4	3.7	6.3
Surplus/(Deficit), $ bn	0.4	0.0	**-2.8**

$4-6 bn is the estimated monthly deficit. Some will be covered by the foreign aid, some will be monetized

…and it is going to get worse

	% of 1/12 of annual plan	**% of March revenue**	**Notes**
Personal income tax	73%	9%	Tax proceeds will likely decline because of lay-offs
Corporate profit tax	232%	26%	CPT was prepaid by some companies, and 2021 profit tax was due in March. Govt has introduced wide STS
VAT	48%	22%	Fuel VAT down from 20% to 7%, local transportation VAT down from 20% to 7%. Import VAT cancelled for 1, 2 and 3 groups of STS.
Dividends from SOEs	803%	31%	SOEs paid dividends in advance; this source of revenue is almost exhausted
NBU profits	n/a	n/a	UAH 19 bn or 78% of the annual plan transferred in February
Other revenues	73%	12%	Excises for fuel and imports, as well as import duties were lifted

POLICY OUTLINE FOR THE FUTURE

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The most difficult policy making in Ukraine’s modern history

Domestic policies

- Restoration of business activities and employment in safer regions of Ukraine.
- Closing the fiscal gap with as little effect on inflation and debt burden as possible
- Massive extraordinary deregulation to be assessed and mainly retailed for the post-war period.
- Logistical issues will demand a lot of hands-on job to build new routes for the exports
- The NBU restrictions on imports and payments abroad might be gradually relaxed

POLICY OUTLINE FOR THE FUTURE

International policies (focused on financial aid)

- Grants instead of loans to ease the debt burden for the post-war future
- Existing debt management should not damage the ability to attract funds immediately and be as less damaging for the country's credibility as possible
- After the war frontloaded Ukraine reconstruction support program should be activated, partly using Russia's frozen assets
- Granting Ukraine the EU Candidate Status will have a profound impact on institutions rebuilding and economic policies.

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