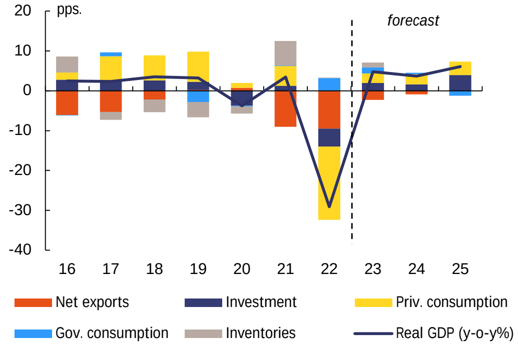
35. UKRAINE

Despite the profound challenges posed by Russia's war of aggression, Ukraine's economy has shown remarkable resilience in 2023, thanks to exceptional harvests, government stimulus underpinned by the unwavering support of international partners, as well as to the authorities' commitment to ensure macrofinancial stability. Growth is forecast to reach 3.7% in 2024 and 6.1% in 2025, with private consumption and public investments as key growth drivers. After declining swiftly in 2023, annual inflation is projected to decrease to 7.6% in 2025, supported by an easing of constraints on production and a tight monetary policy. The fiscal deficit is expected to remain elevated in 2024 driven by high defence expenditures. However, higher nominal GDP growth should increase revenues in 2025 and contribute to a narrowing of the deficit. Public debt is forecast to increase steadily throughout the forecast horizon.

Ukraine's economy proves resilient in 2023

The Ukrainian economy has surprised on the upside throughout 2023 despite continued disruptions in critical infrastructure and supply chains. This better-than-expected performance underscores the adaptability and resilience of Ukrainian consumers and businesses amidst the challenging war environment, which is reflected in improving confidence indicators. In addition, the continuation of the grain deal until July 2023, the EU's solidarity lanes, and exceptionally good harvests supported economic activity. Helped by the strong inflow of international assistance, a sizeable increase in government spending likely contributed to an expansion of domestic demand, too. All in all, GDP growth is set to reach 4.8% in 2023 – a significant upward revision compared to the Spring Forecast.

Graph II.35.1: Ukraine - Real GDP growth and contributions



The economic outlook hinges upon the evolution of the war

Ukraine's economic outlook largely depends on the course of the war, the inflows of foreign funds and the evolution of exports. Under the assumption that conditions are in place for reconstruction efforts to start from the beginning of 2025, real GDP growth is projected to remain moderate in 2024, at 3.7%, before significantly picking up to 6.1% in 2025. Nevertheless, real GDP is set to remain roughly 20% below pre-war levels at the end of the forecast horizon.

Private consumption will likely become the main growth driver, especially in the short term, as consumers continue to adapt to the war environment and a decrease in inflation provides some support to real incomes. Private investment is expected to remain subdued amid heightened uncertainty, but a surge in public investment to kickstart the reconstruction will likely lead to strong total investment growth, particularly in 2025. On the external side, attacks on transport infrastructure and the phasing out of the grain deal have hindered export growth. However, as supply disruptions ease and Ukraine expands the use of alternative export routes, exports are projected to gradually increase. Despite this, net exports are set to contribute negatively to economic growth due to the surge in domestic demand, which results in higher import growth. The current account is forecast to turn into a deficit in 2023 and worsen throughout the forecast horizon, although capital inflows from abroad will likely soften this decrease given the ongoing grant support and the remittances coming from the large number of displaced people outside Ukraine.

This forecast is subject to very high uncertainty, with risks tilted to the downside. An escalation of the conflict could, apart from causing additional human suffering, add to the already high input costs, supply-chain disruptions and lead to further loss of production capacity. An upside risk is that the conditions for the start of reconstruction efforts come earlier than expected, positively impacting investment and exports.

Mismatches in the labour market to keep the unemployment rate high

The labour market has seen signs of stabilization since the beginning of 2023, amid lower net migration outflows and a partial return of internally displaced persons. Nevertheless, the still high level of displaced people abroad and within Ukraine should continue to put pressure on the labour market and contribute to mismatches across regions and sectors. As a result, despite the projected strengthening of economic growth, the unemployment rate is expected to remain elevated throughout the forecast horizon, although on a decreasing trend. At the same time, regional and sectoral shortages of labour and a projected decline of inflation should lead to some recovery in real wages, particularly in 2025.

Inflation set to decrease largely on account of easing supply bottlenecks

Inflation fell to 7.1% in September 2023, down from 26.6% in December 2022. This was largely driven by falling food prices, following a record harvest thanks to exceptionally good weather. Core inflation also moderated on the back of rapid repairs of the energy infrastructure and a tight – albeit easing – monetary policy. Under the assumption of further easing supply constraints and decelerating global prices, inflation is expected to decline visibly throughout the forecast horizon.

Fiscal deficit to decrease but remain high

After increasing in 2023, the general government deficit is set to remain elevated in 2024 due to, on the expenditure side, high expenditures related to the war effort, and on the revenue side, weak revenue growth coming from a still low GDP increase. In 2025, total expenditure should see some decrease due to lower war-related expenditures, contributing to some narrowing of the fiscal deficit. Public debt is expected to increase to just below 100% of GDP by 2025.

Table II.35.1:

Main features of country forecast - UKRAINE

	2022		Annual percentage change						
bn UAH	Curr. prices	% GDP	04-19	2020	2021	2022	2023	2024	2025
GDP	5189.6	100.0	:	-3.8	3.4	-29.1	**4.8**	**3.7**	**6.1**
Private Consumption	3404.7	65.6	:	1.7	6.8	-26.7	**3.7**	**4.0**	**5.4**
Public Consumption	1985.6	38.3	:	-0.7	0.8	18.0	**3.9**	**1.0**	**-3.2**
Gross fixed capital formation	597.1	11.5	:	-21.3	9.3	-34.3	**17.0**	**12.0**	**28.0**
Exports (goods and services)	1842.1	35.5	:	-5.8	-8.6	-42.4	**-2.5**	**3.3**	**8.5**
Imports (goods and services)	2715.7	52.3	:	-6.4	14.2	-18.4	**2.7**	**3.8**	**5.5**
GNI (GDP deflator)	5462.3	105.3	:	-2.9	-1.7	-23.2	**2.9**	**2.9**	**5.5**
Contribution to GDP growth: Domestic demand			2.9	-2.7	6.4	-19.7	**5.9**	**4.6**	**6.1**
Inventories			-0.7	-1.8	6.1	0.1	**1.2**	**0.0**	**0.0**
Net exports			-2.2	0.7	-9.1	-9.5	**-2.3**	**-0.9**	**0.0**
Employment			:	-4.0	-2.4	-18.5	**-2.7**	**0.9**	**2.8**
Unemployment rate (a)			8.8	9.5	9.9	18.6	**17.8**	**16.2**	**14.5**
Compensation of employees / head			:	-	-	-	**-**	**-**	**-**
Unit labour costs whole economy			:	-	-	-	**-**	**-**	**-**
Saving rate of households (b)			:	-	-	-	**-**	**-**	**-**
GDP deflator			:	10.3	24.8	34.3	**19.4**	**15.6**	**12.1**
Consumer price index			:	2.7	9.4	20.2	**13.5**	**7.7**	**7.6**
Terms of trade goods			:	11.2	23.2	-0.9	**-3.3**	**3.0**	**2.9**
Trade balance (goods) (c)			-7.4	-4.3	-3.3	-12.7	**-14.5**	**-13.5**	**-12.3**
Current-account balance (c)			-2.7	3.3	-1.9	4.1	**-4.3**	**-6.0**	**-6.5**
General government balance (c)			-2.6	-5.2	-3.4	-16.3	**-20.5**	**-19.7**	**-12.0**
Structural budget balance (d)			:	-	-	-	**-**	**-**	**-**
General government gross debt (c)			61.2	60.6	47.7	77.4	**87.0**	**96.2**	**98.3**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.