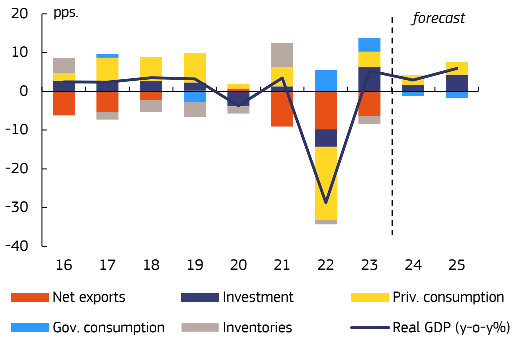
36. UKRAINE

Ukraine's economy continues to grapple with the impact of Russia's war of aggression. After showing strong resilience in 2023, growth is set to decelerate in 2024 due to weaker sentiment, the renewed destruction of energy infrastructure by Russian attacks, and labour shortages. However, under the technical assumption that conditions for a gradual increase in early reconstruction efforts will be in place from early 2025, GDP growth should then gather pace. Increasing labour costs, supply disruptions, and a recovery in domestic demand are expected to keep inflation high in 2024 and 2025. Sizeable revenue measures introduced by the government are expected to only moderately ease the fiscal deficit in 2024, which is forecast to remain elevated due to large war-related expenditures.

Economic growth proved resilient in 2023 but is expected to decelerate in 2024

Despite continued Russian attacks, the Ukrainian economy grew by 5.3% in 2023. This strong performance was underpinned by a robust agricultural output, supportive fiscal policy bolstered by international aid inflows, as well as the gradual adaptation of consumers and businesses to wartime conditions.

Graph II.36.1: **Ukraine - Real GDP growth and contributions**



Real GDP growth is projected to decelerate significantly in 2024. The war will continue to dampen sentiment and hinder productive capacities, including in the energy sector, where early estimates suggest that between 30-40% of energy generating capacity was destroyed in early 2024. The ongoing conscription of individuals, coupled with the sustained displacement of persons fleeing the war both internally and abroad, will likely continue to generate labour shortages and have repercussions for economic output.

Looking at the demand components of growth, private consumption is set to decelerate due to dampened sentiment but become the main driver in 2024, supported by declining inflation, robust wage growth reflecting acute labour shortages, and a decrease in the unemployment rate. Investment is set to continue benefitting from spending both in defence and the construction sector, although heightened uncertainty will keep restraining overall private investment growth. On the external side, the revival of the Black Sea transport route will likely bolster exports, resulting in a gradual improvement in the negative contribution of net exports to GDP growth. However, the trade balance should remain in negative territory, given the large import needs for recovery, reconstruction and defence.

Under the assumption that conditions for a gradual increase in early reconstruction efforts will be in place from early 2025, growth is forecast to pick up in 2025 following a boost in confidence and large reconstruction investments. As a result, after decelerating to a projected 2.9% in 2024, real GDP growth is expected to gather pace and reach 5.9% in 2025.

This forecast is of course subject to particularly high uncertainty, with risks largely tilted to the downside. An escalation of the conflict could, apart from causing additional human suffering, add to the already high input costs and lead to further loss of production capacity. An increase in the number of people fleeing the war could also exacerbate labour market pressures and weigh on domestic demand.

War-related disruptions in the labour market to keep the unemployment rate high

The labour market has seen some signs of stabilisation since 2023, amid lower net migration outflows and a partial return of internally displaced persons. However, the still high number of displaced persons, both abroad and within Ukraine, is set to continue labour market disruptions and contribute to mismatches across regions and sectors. This will act to keep the unemployment rate high throughout the forecast horizon. At the same time, the decline of inflation should lead to a sizeable recovery in real wage growth, both in the private and public sectors.

Inflation set to increase gradually following a marked drop in 2023 and early 2024

Inflation has recorded a large and steady decline since 2023, reaching 3.2% in March 2024, down from 21.3% in March 2023. This large drop was mainly driven by declining food prices, which were pushed down by an oversupply of agricultural products in the domestic market in view of the strong harvest and disruptions to the export routes. As this factor gradually fades, inflation is expected to increase, also driven by disruptions in energy supply, increasing labour costs, and a recovery in domestic demand. Consequently, after decreasing to 5.5% in 2024, inflation is expected to pick up to 7.8% in 2025.

Public deficit to remain high but to gradually decrease

The general government deficit increased to 19.7% in 2023. This was driven by a large increase in defence expenditure, which accounted for roughly 40% of total expenditure. In 2024, spending in non-defence categories has been tightly constrained, reflecting the priority of the war effort. This is expected to result in total expenditure falling as a percentage of GDP. Total revenue is set to benefit from measures such as the tax on extraordinary profits in the banking sector (1% of GDP) and the expiration of the tax reduction on fuel and tobacco (1.6% of GDP), as well as the continued recovery in nominal GDP. Consequently, the fiscal deficit is expected to narrow to 17.7% in 2024. In 2025, the projected strengthening in economic activity should propel tax revenues, while the expenditure side should reflect the reallocation of expenditure towards rehabilitation investments leading to a narrowing of the fiscal deficit. Public debt is projected to increase further given the large financing needs and the increased use of domestic financing at elevated rates, albeit at a slowing pace and remaining below the threshold of 100% of GDP.

Table II.36.1:

Main features of country forecast - UKRAINE

		2023		Annual percentage change						
	bn UAH	Curr. prices	% GDP	04-19	2020	2021	2022	2023	2024	2025
GDP		6537.8	100.0	:	-3.8	3.4	-28.8	**5.3**	**2.9**	**5.9**
Private Consumption		4191.5	64.1	:	1.7	6.8	-27.5	**6.1**	**3.9**	**5.3**
Public Consumption		2725.2	41.7	:	-0.7	0.8	31.4	**9.0**	**-2.6**	**-4.3**
Gross fixed capital formation		1104.7	16.9	:	-21.3	9.3	-33.9	**52.9**	**9.8**	**23.5**
Exports (goods and services)		1868.9	28.6	:	-5.8	-8.6	-42.0	**-5.4**	**6.0**	**9.1**
Imports (goods and services)		3237.0	49.5	:	-6.4	14.2	-17.4	**8.5**	**3.8**	**5.5**
GNI (GDP deflator)		6739.4	103.1	:	-2.9	-1.7	-22.7	**3.1**	**2.2**	**5.4**
Contribution to GDP growth:	Domestic demand			2.9	-2.7	6.4	-17.9	**13.8**	**3.1**	**5.9**
	Inventories			-0.7	-1.8	6.1	-1.1	**-2.2**	**0.0**	**0.0**
	Net exports			-2.1	0.7	-9.1	-9.8	**-6.3**	**-0.2**	**0.0**
Employment				:	-4.0	-1.9	-31.5	**-1.6**	**3.9**	**8.5**
Unemployment rate (a)				8.8	9.5	9.9	24.3	**19.2**	**15.5**	**14.1**
Compensation of employees / head				:	:	:	:	**:**	**:**	**:**
Unit labour costs whole economy				:	:	:	:	**:**	**:**	**:**
Saving rate of households (b)				:	:	:	:	**:**	**:**	**:**
GDP deflator				:	10.3	24.8	34.9	**18.5**	**15.8**	**7.5**
Consumer price index				12.7	2.7	9.4	20.2	**12.8**	**5.5**	**7.8**
Terms of trade goods				:	11.1	23.2	0.4	**-3.0**	**3.0**	**2.9**
Trade balance (goods) (c)				-7.1	-4.3	-3.3	-9.5	**-16.1**	**-14.5**	**-13.9**
Current-account balance (c)				-2.7	3.3	-1.9	4.9	**-5.1**	**-6.4**	**-7.5**
General government balance (c)				-2.6	-5.4	-3.3	-15.3	**-19.7**	**-17.7**	**-8.7**
Structural budget balance (d)				:	:	:	:	**:**	**:**	**:**
General government gross debt (c)				43.0	60.5	48.9	77.7	**84.4**	**94.4**	**97.8**

(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.