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Economic Consequences of the Ukraine Conflict

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Outline

- Consequences for Ukraine
- Consequences for Russia
- Consequences for the EU
- Sanctions and their impacts

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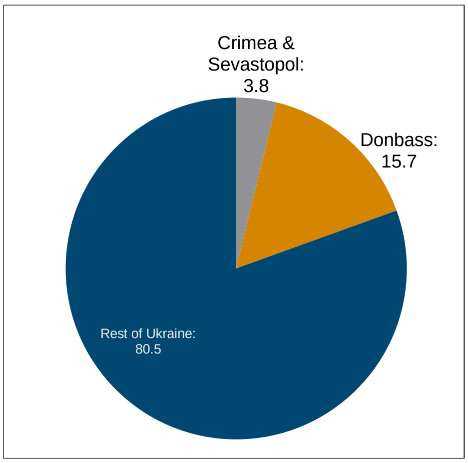
Consequences for Ukraine

Gross regional product

2012, in % of total

- the role of Crimea is modest
- but Donbass:
  - 16% of Ukraine's GDP
  - 6.5 million population
  - home to coal-mining and metallurgy

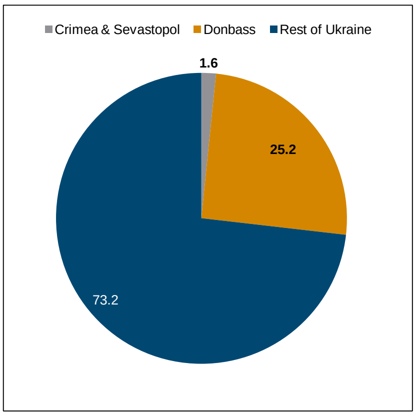


Source: wiiw based on national statistics.

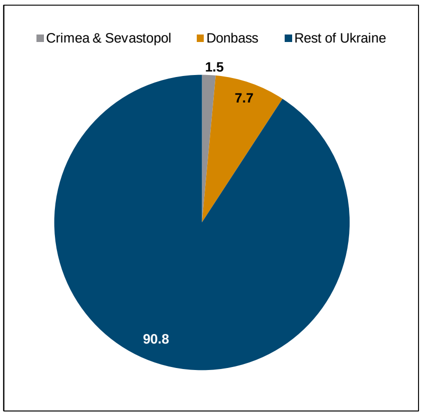
Foreign trade by region

2013, in % of total

Exports of goods

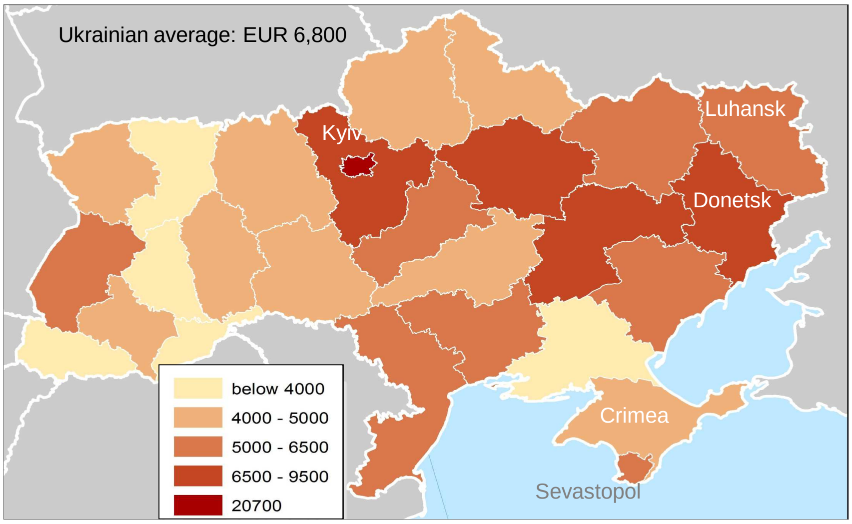


Imports of goods



Source: wiiw based on national statistics.

GDP per capita, EUR at PPP, 2012



Source: wiiw based on national statistics.

Economic costs of the war in Donbass

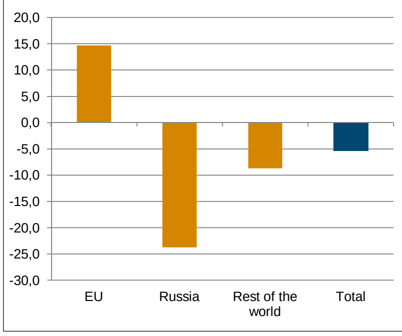
- Economic damage currently estimated at USD 7-8 billion (6% of GDP)
- Industrial production in August 2014 dropped by
  - 60% in Donetsk and 85% in Luhansk (year-on-year)
  - largely on account of power cuts and railway disruptions
- Over 1 million refugees
  - including some 320 thousand to other regions of Ukraine
  - and nearly 900 thousand to Russia
  - may undermine long-term recovery prospects

Economic prospects

- This year: 8-10% GDP recession
  - war-related destructions in Donbass
  - restrictions on military and dual-use goods exports to Russia
  - inflation erodes purchasing power
  - investments collapse
- Prospects for stabilisation highly uncertain
  - conflict settlement crucial

Exports dynamics in January-July 2014

% change year-on-year



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Consequences for Russia

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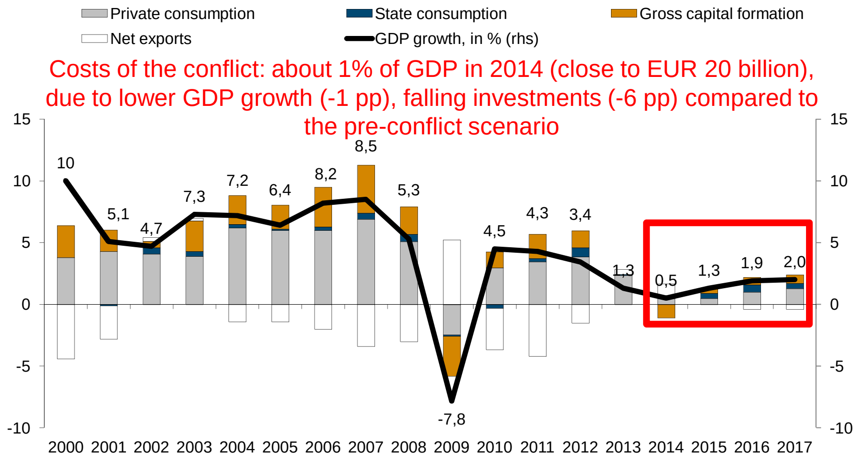
GDP growth: current (realistic) scenario; contributions of main components to GDP growth, in pp



Source: wiiw Annual Database, national statistics, own estimates.

Russia was 'stuck in transition', economy close to stagnation already before Ukraine crisis. Key challenges (old and new):

- Energy exports and growth sustainability
  - Increased pressures on energy supply diversification (both in the EU and RU)
  - Sectoral sanctions already start to bite, no longer largely symbolic
  - Investment climate already suffers, imports and FDI down, capital flight
- Diversification and modernisation of the economy under threat
  - Growing reform pressures owing to sanctions?
  - Yet modernisation is more difficult without more FDI!
- Stability of the ruling elite
  - Putin's ratings grow, Russia's ratings fall, rouble and MICEX fluctuate
  - Yet this may change with more hardship …
- Integration on the post-Soviet space derailed/fails?
  - Crimea not really helpful for Putin's Eurasia integration project
  - New design/reset of EU neighbourhood policies?

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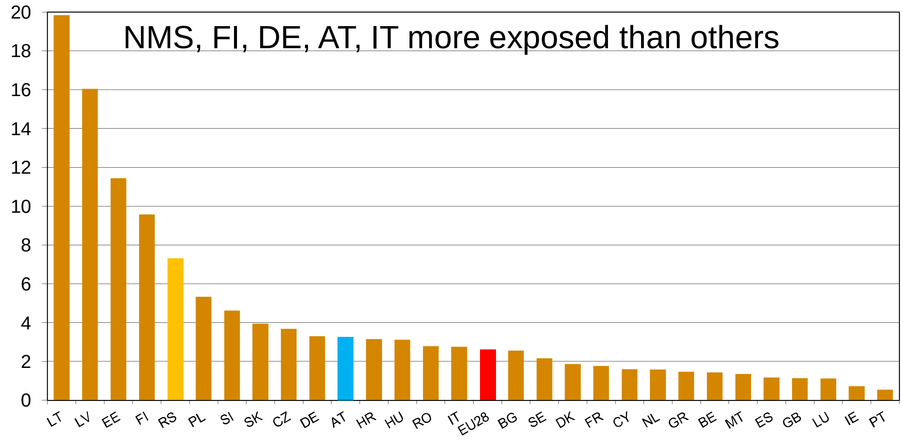
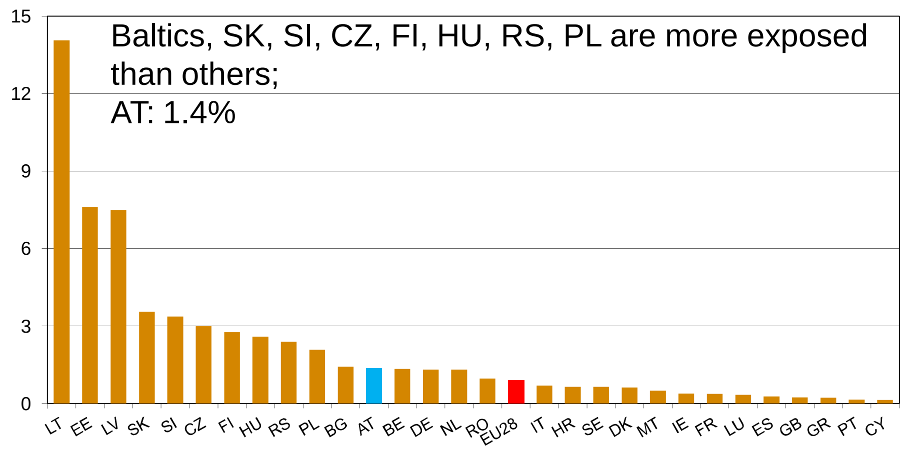
Consequences for the EU

Share of Russia in EU goods exports, in % of total, 2013



Source. wiiw Annual Database, EU Comext.

Share of goods exports to Russia in % of GDP, 2013



Source: wiiw Annual Database, EU Comext.

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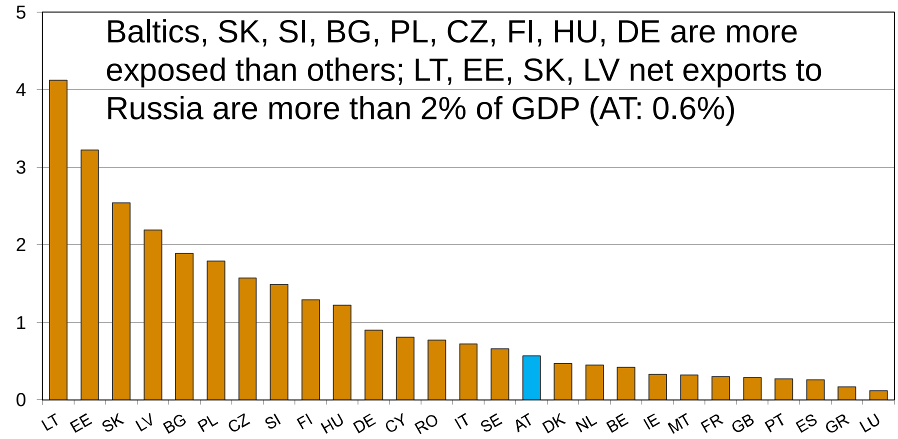
Share of domestic value added of exports to Russia in % of GDP, 2013 (estimated)



Source: EU Comext, WIOD, own estimates.

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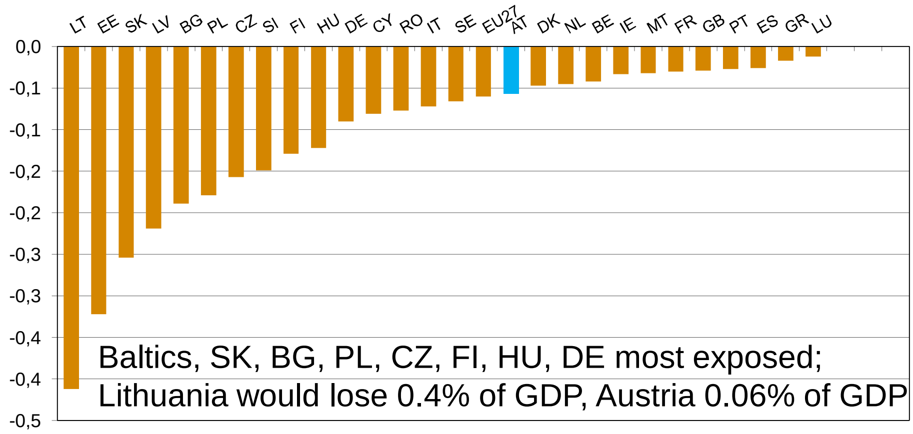
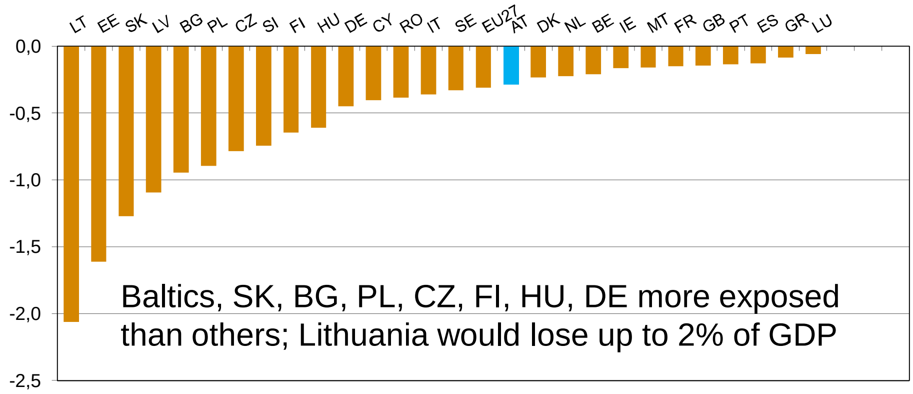
Scenario (Ia): estimated loss of GDP (in %) if domestic value added of exports to Russia drops by 10%



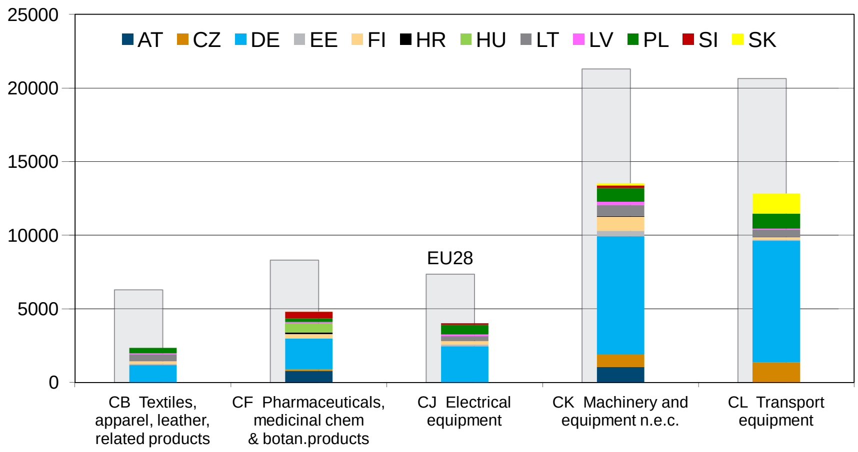
Source. Own estimates based on wiiw Annual Database, EU Comext.

Scenario (IIa): estimated loss of GDP (in %) if domestic value added of exports to Russia drops by 50%



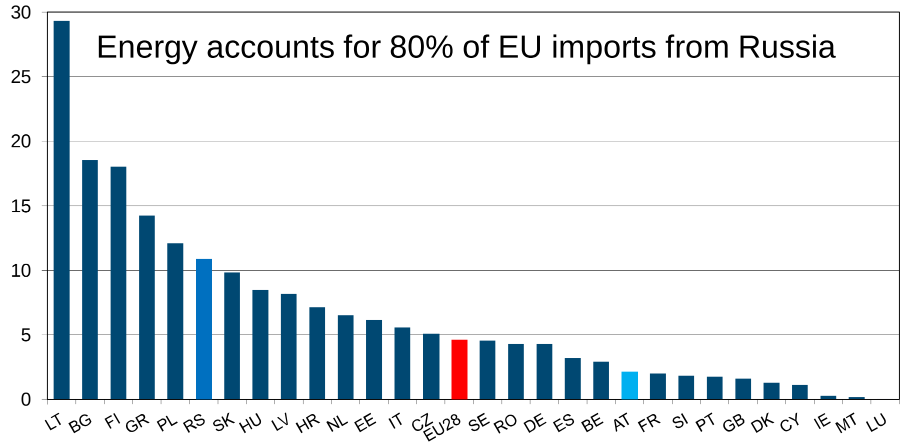
Source: Own estimates based on WIOD Database, EU Comext.

EU export exposure to Russia: 5 key industries and 12 major exporting countries, EUR mn, 2013



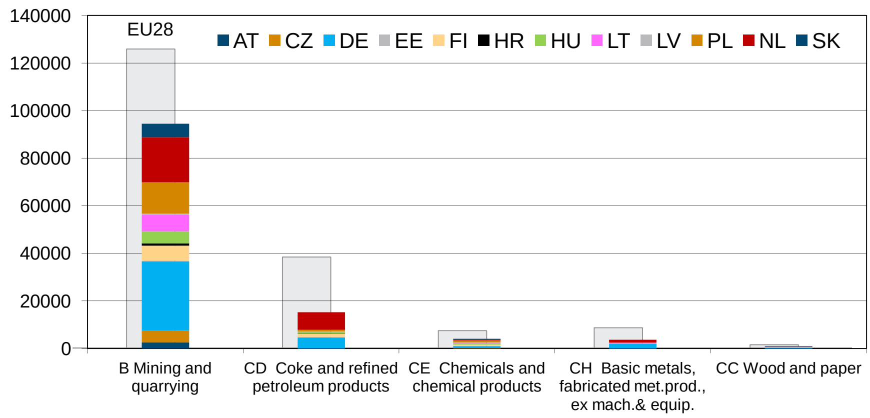
Source. wiiw Annual Database, EU Comext.

Share of Russia in goods imports, in % of total, 2013



Source: wiiw Annual Database, EU Comext.

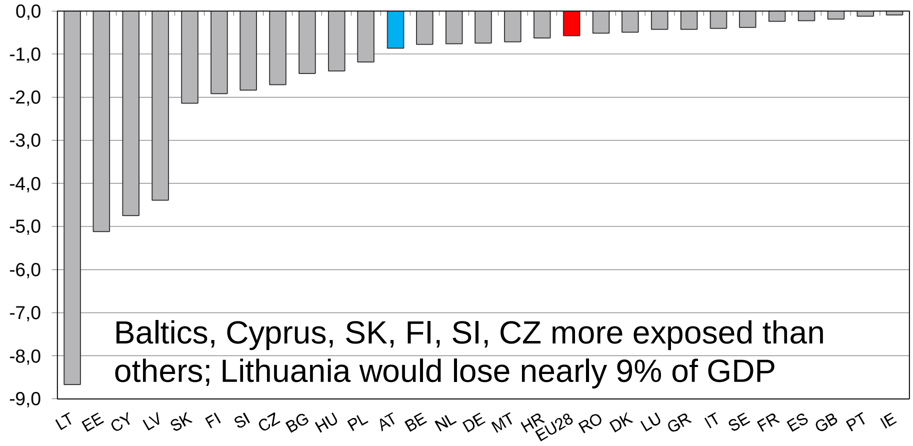
EU import exposure to Russia: 5 key industries and 12 major importing countries, EUR mn, 2013



Oil and gas: Austria, Germany and the Netherlands estimated.

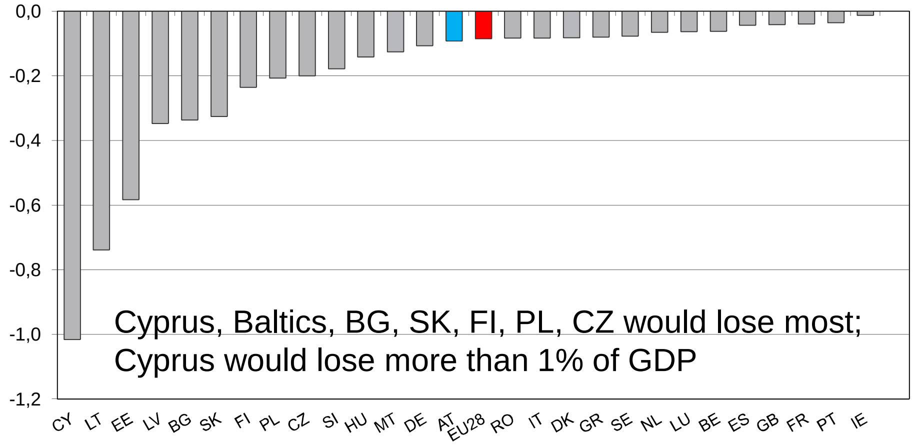
Source: wiiw Annual Database, EU Comext.

Scenario (II): estimated GDP loss (in %) if exports (both goods and services) to Russia drop by 50%



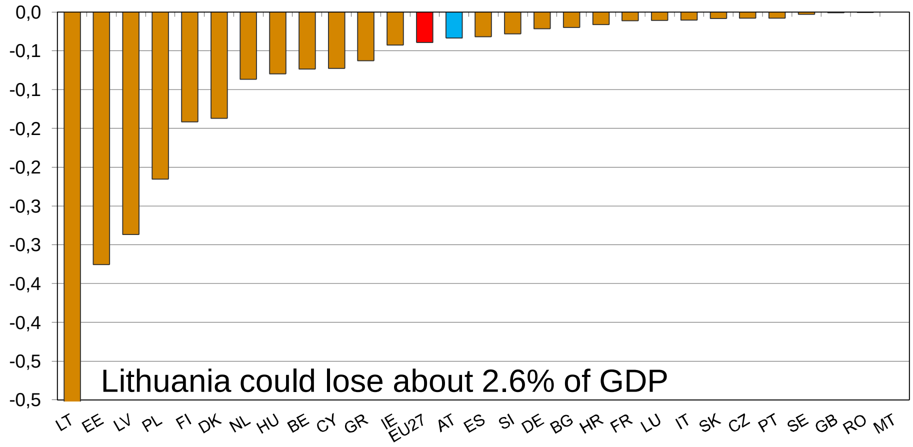
Source. Own estimates based on wiiw Annual Database, EU Comext.

Scenario (I): estimated GDP loss (in %) if domestic value added of goods and services exports to Russia drops by 10%



Source. Own estimates based on wiiw Annual Database, EU Comext.

Estimated GDP loss (in %) resulting from Russia's August 2014 food import ban



Source. Own estimates based on wiiw Annual Database, (*http://ec.europa.eu/agriculture/statistics/trade/2012/annex4 en.pdf*).

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Sanctions and their impacts

Western sanctions and their impacts (I)

- Sanctions unlikely to have desired effects – whatever these might be (change Russian behaviour?)
- But sanctions still painful for all sides (UA, RU, EU)
- Russia retaliates, some EU countries suffer more
- Russian investment and GDP growth down
- Import substitution and export diversion
- Capital flight, exchange rate fluctuation and inflation
- Russia turning inwards and even more assertive?
- Greater medium-term reform pressures?

Western sanctions and their impacts (II)

- Eurasian integration derailed?
- Lasting damage to East-West relations
- Serious medium- and long-term repercussions on Russian growth, living standards and stability
- Trade and energy supplies diversification
- Russian modernisation hampered without more FDI, technology imports and better East-West relations
- What about Ukraine, Crimea and Novorossia?
- Sanctions' effectiveness versus impact

Thank your for your attention!

Country codes

AT	Austria	IE	Ireland
BE	Belgium	IT	Italy
BG	Bulgaria	LT	Lithuania
CY	Cyprus	LU	Luxembourg
CZ	Czech Republic	LV	Latvia
DE	Germany	MT	Malta
DK	Denmark	NL	Netherlands
EE	Estonia	PL	Poland
ES	Spain	PT	Portugal
FI	Finland	RO	Romania
FR	France	RS	Serbia
GB	Great Britain	SE	Sweden
GR	Greece	SI	Slovenia
HR	Croatia	SK	Slovakia
HU	Hungary		
NMS	New Member States	RoW	Rest of the World