The economics of the Russia-Ukraine war

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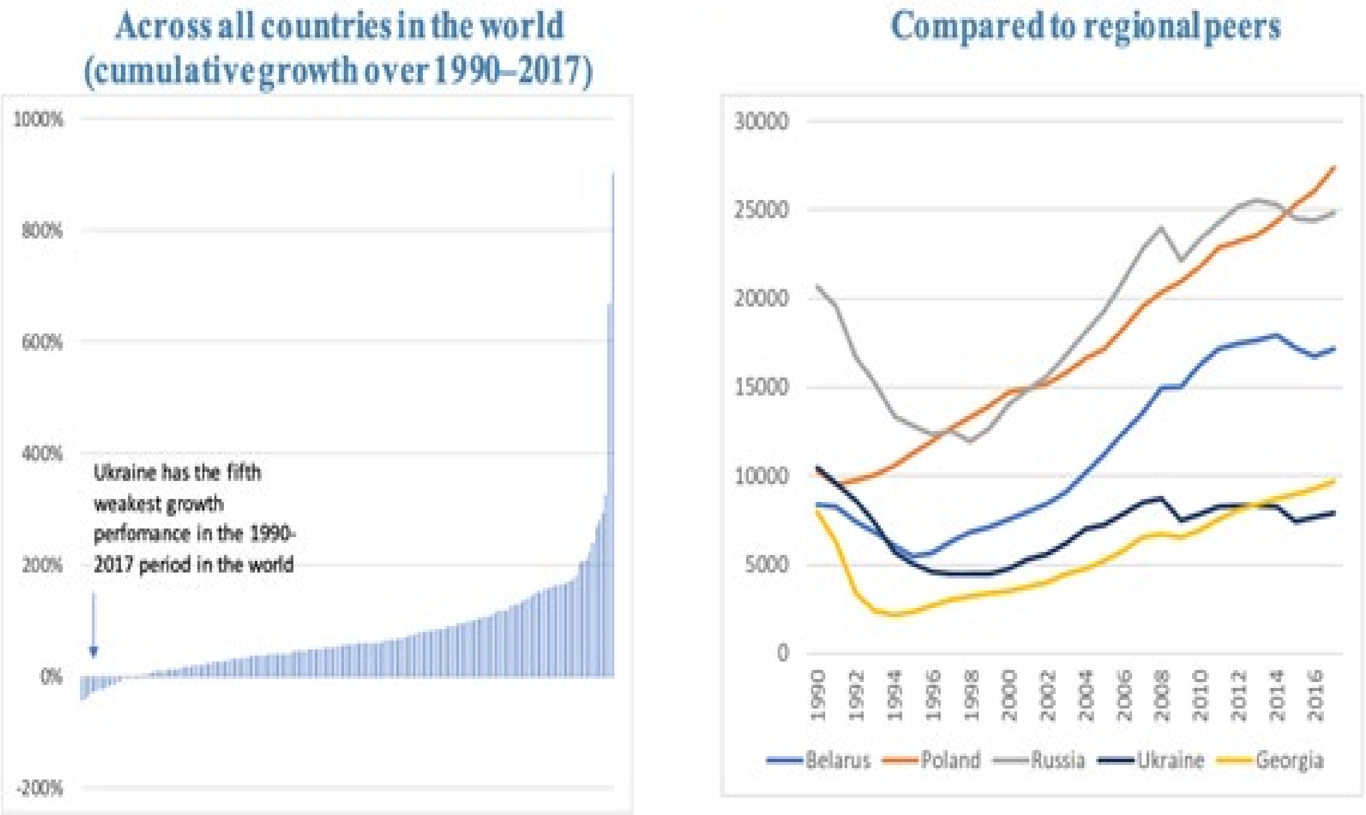
Post-Soviet performance

Figure 1. Ukraine's GDP per capita growth 1990–2017



Source: WDI, GDP per capita in PPP (2011 international $)

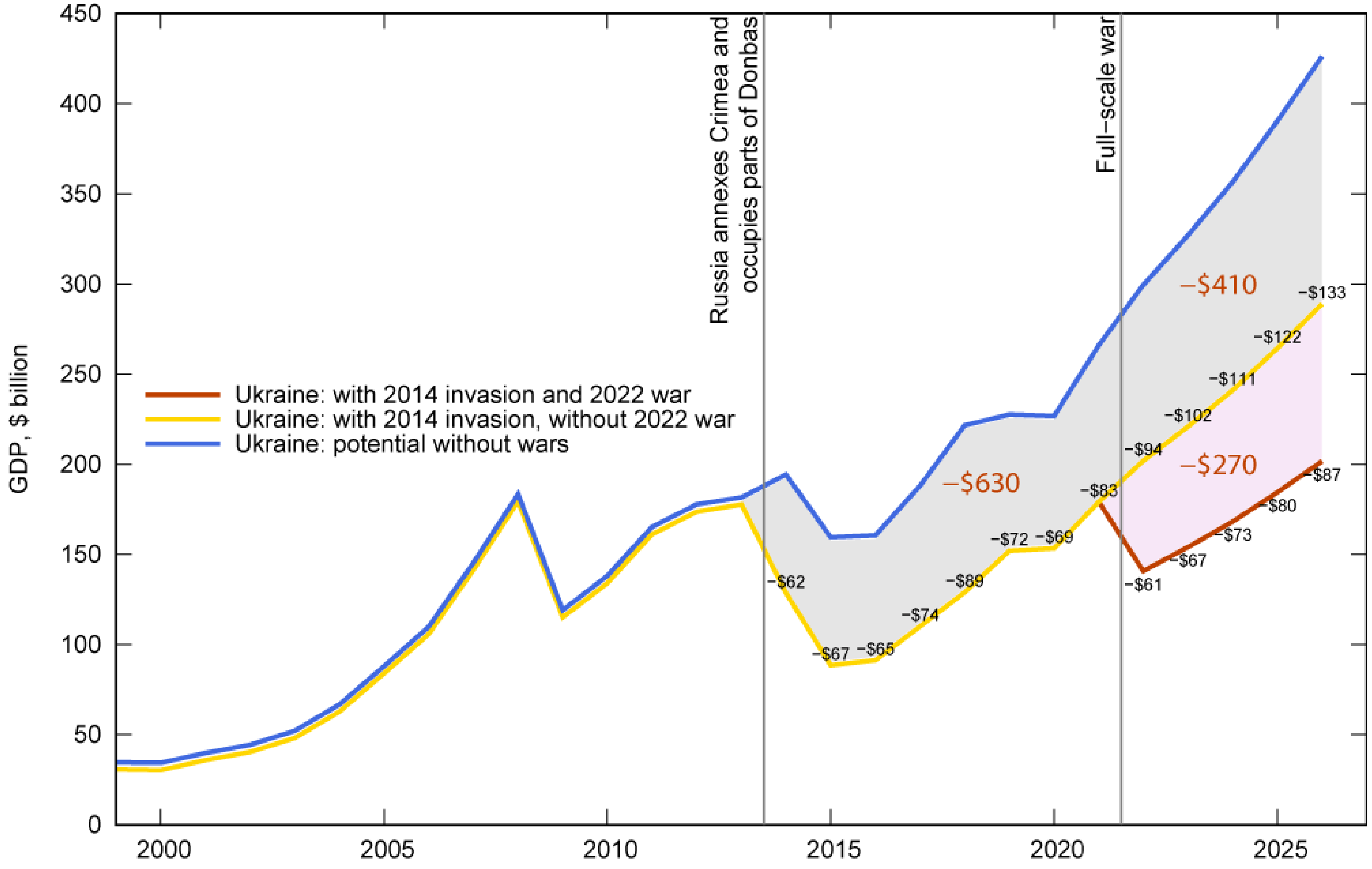
All the former Soviet satellites took a long time to recover GDP per head and income levels, but in the case of Ukraine it has never got back to the 1990 level. **Ukraine's performance between 1990 and 2017 was not just worse than its European neighbours. It was the fifth-worst in the entire world**. Between 1990 and 2017 there were only 18 countries with negative cumulative growth and even in that select group, **Ukraine's performance puts it in the bottom third along with the Democratic Republic of Congo, Burundi and Yemen.**

Damage to Ukraine: huge!

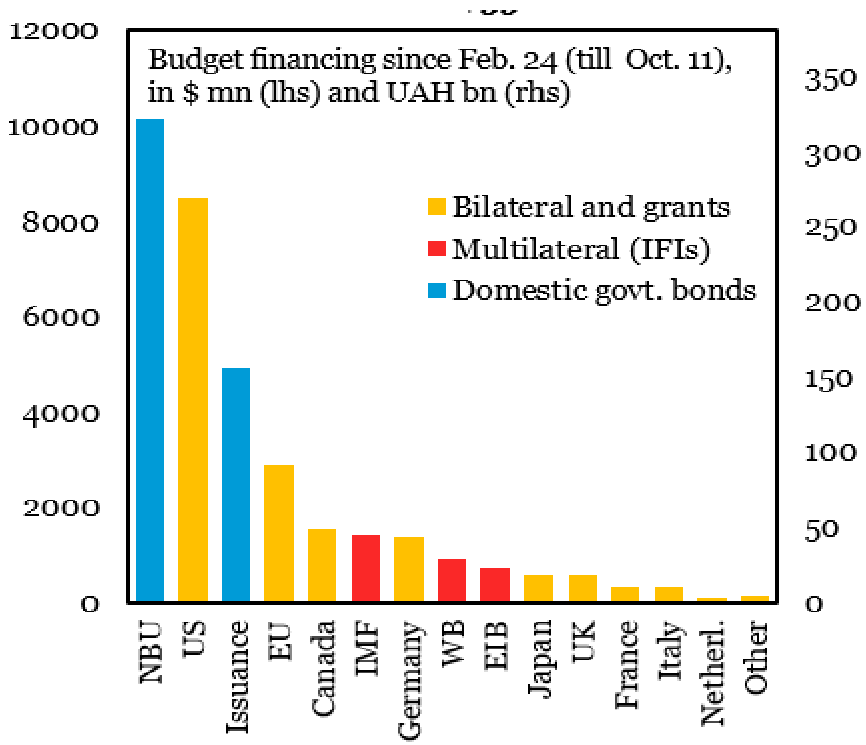
What is the damage to the Ukraine economy from the Russian invasion?

One Ukrainian economist estimates the damage from the 2014 and 2022 wars as equivalent to $1.36 trillion. Of this number, $680 billion are losses incurred between 2014 and 2021, $155 billion of losses are expected in 2022, and the remaining $525 billion during 2023-2026.

This assumes that Ukraine's GDP falls only 30% this year - it could be worse.



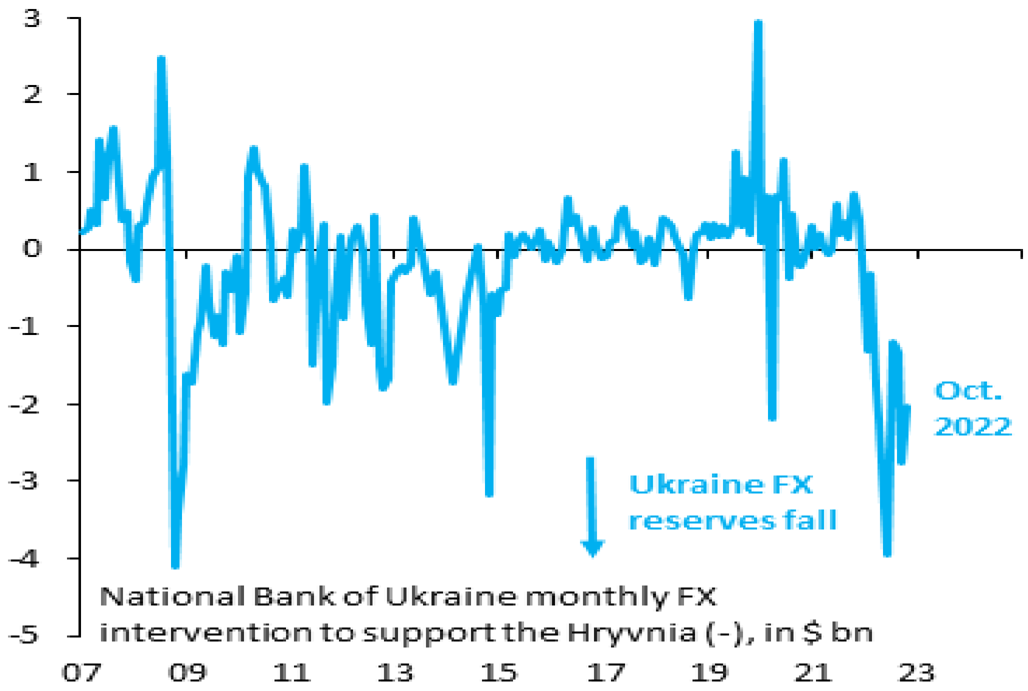
Foreign funding still not enough



Source: Ministry of Finance, IIF

Foreign funding covers only a fraction of the resulting deficit. Local investors are not keen to buy Ukrainian local-currency bonds, on account of inflation. So borrowing from the central bank, the NBU, i.e. printing money has become the last resort of (inflationary) war finance

Ukraine lost -$19 bn in reserves since the invasion.



A Marshall plan?

- To restore the Ukraine economy and rebuild is likely to cost $500bn minimum, say over the next five years. That's about 1.0% of EU GDP per year or 0.75% of G7 GDP – at a minimum.
- $13bn in 1948 was about 1.1% of US GDP then and is equivalent to about $130bn now. So any Marshall Plan for Ukraine would have to deliver double that, as shared between the US and Europe.
- The 1948 plan was composed of both outright grants and loans. The aid accounted for about 3% of the combined GDP of the recipient countries between 1948 and 1951, which meant an increase in GDP growth of less than half a percent. Ukraine will need much more.

Rebuilding Ukraine: the Russian obstacle

- The war has already led to Russian forces gaining control of at least $12.4trn worth of Ukraine's resources in energy (cola), metals and mineral deposits, apart from agricultural land. If Putin's forces succeed in annexing Ukrainian land seized during Russia's invasion, Kyiv would permanently lose almost two-thirds of its deposits. Moscow now controls 63% of Ukraine's coal deposits, 11% of its oil, 20% of its natural gas, 42% of its metals, and 33% of its rare earths.
- So any rebuilding effort funded by Western capital has a major obstacle. *"Not only will Ukraine have lost a lot of its territory and its resources, but it would be constantly vulnerable to another onslaught by Russia,"* said Jacob Kirkegaard, a fellow at the Washington-based Peterson Institute for International Economics.
- *"No one in their right mind, a private company, would invest in the rest of Ukraine if this were to become a frozen conflict."* Ukraine has suffered continual bombing and military attacks with thousands of civilians dying and millions having to flee their homes and even leave the country. If Russia maintains its control of existing gains, the reconstruction of Ukraine as an independent state based funded by Western capital is put in jeopardy.

The neoliberal plan for Ukraine

The IMF is insisting, with the support of the latest post-Maidan government, to carry out substantial privatisation of the banks and state enterprises in the interests of ‘efficiency’ and to control ‘corruption’.

Most significant has been the move to privatise land holdings. The government was resisting allowing foreigners to buy land. But in 2024, Ukrainian legal entities will qualify for transactions involving up to 10,000 hectares and will apply to an agricultural area of 42.7 million hectares (103 million acres). That is equivalent to the entire surface area of the state of California, or all of Italy!

The World Bank is positively drooling at this opening up of Ukraine’s key industry to capitalist enterprise: *“This is without exaggeration a historic event, made possible by the leadership of the President of Ukraine, the will of the parliament and the hard work of the government.”* So Ukraine plans to open up its economy even more to capital, particularly foreign capital, in the hope that this will deliver faster growth and prosperity.

The West’s economists speak

- **“Although wartime governments usually take over the allocation of resources, Ukrainian circumstances call for more market-based allocation mechanisms to ensure cost-effective solutions that do not overburden the state capacity, exacerbate existing problems (such as corruption), or encourage (untaxed) black market activities. To this end, the aim should be to pursue extensive radical deregulation of economic activity, avoid price controls, and facilitate a productive reallocation of resources.”**
- “To this end, the government should minimise regulation and other red tape that can constrain or slow down the reallocation of labour, capital, and materials in the economy. On balance, market-based allocations are preferred.”
- **”The government should dramatically loosened labour market regulations ... Land regulation, access to electricity, and other infrastructure should be streamlined to allow easier reallocation for firms. … Perhaps, the government can appoint a high-level official (e.g. ‘deregulation chief’) to coordinate and push for deregulation.”**

Ukraine government policy

- Economy minister Rodnyansky, who is also a professor of economics at the University of Cambridge, said “receiving more foreign aid is the easiest way to fund the war”; however, efforts must be made to cut spending, collect taxes and issue debt to finance its efforts. “We have deep issues with our labour code, developed in the 1970s, that needs to be overhauled.” **We’re going to try to emulate a more liberal approach, like Denmark, with a flexible labour market because we need to catch up.”**

- Legislation that was signed into law by Zelenskiy at the end of August effectively removes 70-80 per cent of the country’s workforce—employees of small- and medium-sized enterprises—from the protection of national labour law. **Ukrainian labour lawyer and activist George Sandul described the final goal of the draft reconstruction plans as a ‘Mad Max-style dystopia’ where ‘everybody will negotiate on their own without any rules**

- Rodnyansky said he was also in favour of reviewing minimum wages to scrap them in some industries where it did not increase employment. **“We need to make sure it’s not too high because our economy is collapsing and we need to make sure it does not push up unemployment**,” he said.

Russia: crony capitalism to autocracy

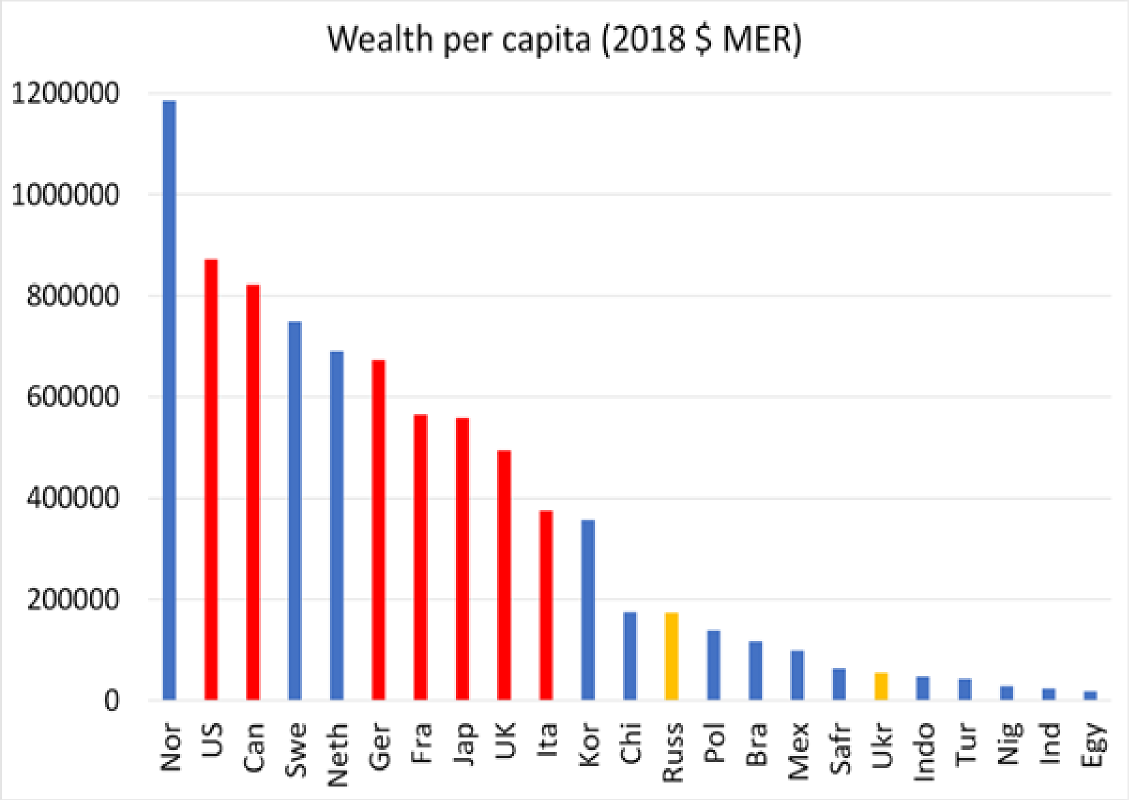
- When the Soviet Union collapsed in the early 1990s, the elite in Russia, with the enthusiastic backing of US imperialism and Western economic advisers, moved quickly to dismantle the Soviet state sector. There was no attempt to introduce even 'liberal democracy'. Much more important was to gain control of Russia's resources and labour for private profit. .
- Economic failure crippled the Yeltsin government and led to Yeltsin stepping down as president just over a year later. Yeltsin made way for his prime minister Vladimir Putin. Putin, a former KGB officer, promised to establish stability and prosperity with reforms.
- Step-by-step Putin created a state of crony capitalism that was bolstered by the so-called *siloviki*—powerful figures from the security and military services—who were active participants in Putin's increasingly corrupt system.
- Amid stagnation, inequality has accelerated: *"the wealthiest 3 percent of Russians owned 89 percent of all financial assets in 2018."* The *Moscow Times* reports *"the number of billionaires in Russia grew from 74 to 110 between mid-2018 and mid-2019, while the number of millionaires rose from 172,000 to 246,000." According to Forbes's rating, the total wealth possessed by Russia's top 200 in 2019 was $15 billion higher than it had been in 2014.*

Russian “imperialism”: a paper bear

- Putin may think Russia can be an imperialist power, but the economic reality is that Russia is just a large peripheral economy outside the US-led imperialist bloc like Brazil, China, India, South Africa, Turkey, Egypt etc – if with a larger military than most.

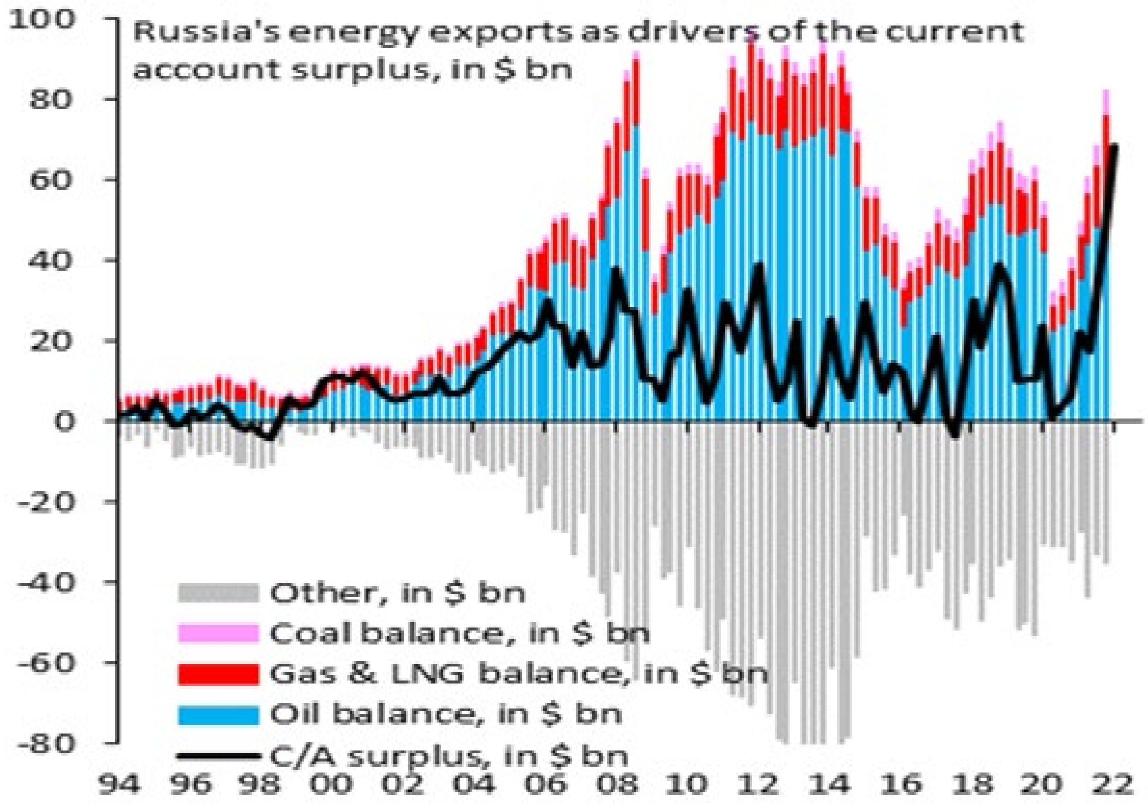
The irony is that Putin’s imperialist ambitions for control of the peripheral countries of the former Soviet Union are not backed up by a modern imperialist economy.

Russia is no super power, economically or politically. Its total wealth (including labour and natural resources) is way down the league compared to the US and the G7 (red bars). And even its supposed military might has been exposed as a paper tiger (bear).



Russian economy: the sanctions weapon

- The French finance minister said that *“[w]e are waging total economic and financial war against Russia, Putin, and his government”*
- Energy sanctions exempted
- Gradual ending of Russian energy to Europe (gas and oil)
- Diversion of energy exports to Asia
- Longer term: no FDI and a technology ban



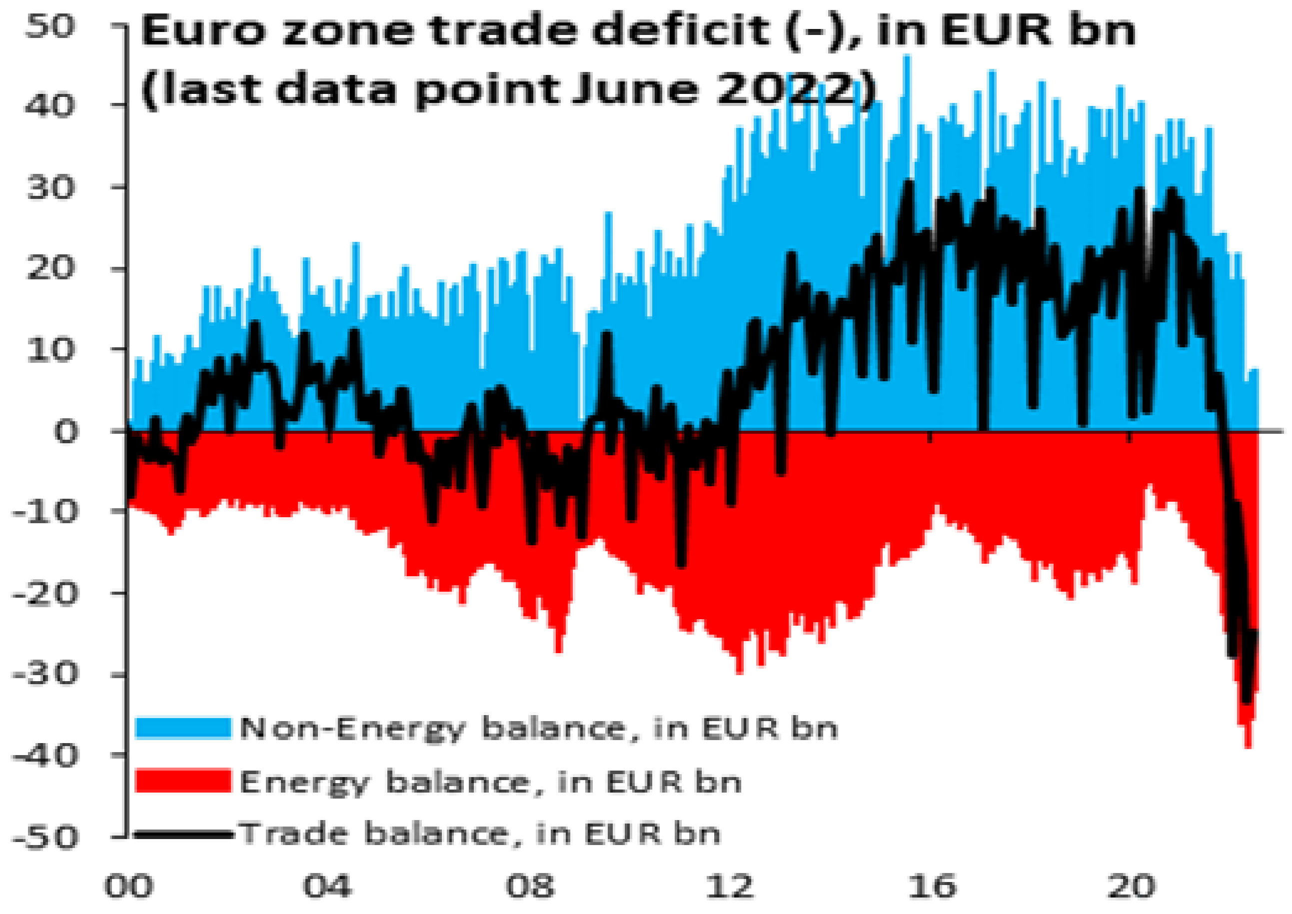
Ukraine – Russia: an earthquake

“The war in Ukraine is like a powerful earthquake that will have ripple effects throughout the global economy, especially in poor countries” IMF

Global impact: the cost of living crisis

Energy and food prices rocket hitting the global south countries the hardest

But also, Europe with energy, particularly Germany, the powerhouse of European manufacturing



Recession ahead?

Jacob Frenkel, head of the Group of 30 consortium of global policy makers, summed it up:

“We have the energy crisis, we have the food crisis, we have the supply chain crisis and we have the war, all of which has profound implications for the economic performance of the world’.

And the IMF notes,

“The global outlook has already darkened significantly since April. The world may soon be teetering on the edge of a global recession, only two years after the last one.”

Two blocs and shocks

‘Liberal’ economist Wolf, is deeply worried. *“A new world is being born. The hope for peaceful relations is fading…. No one knows what will happen. But we do know this looks to be a disaster…….The combination of war, supply shocks and high inflation is destabilising, as the world learnt in the 1970s. Financial instability now seems very likely, too. A prolonged bout of stagflation seems certain, with large potential effects on financial markets.”*

In the long term, the emergence of two blocs with deep splits between them is likely, as is an accelerating reversal of globalisation and sacrifice of business interests to geopolitics. Even nuclear war is, alas, conceivable.”

Ukraine: a dress rehearsal?