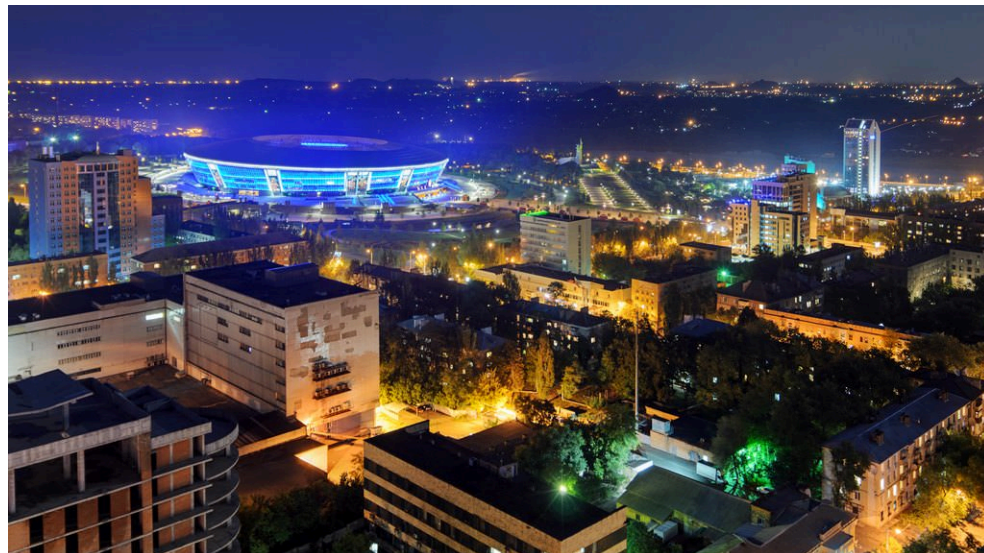


# Ukraine Watch: War shock is reflected in a record 37.2% yoy GDP drop in Q2'2022

According to an operative estimate, real GDP decreased by 37.2% yoy and 19.1% qoq. The record drop was reasonably expected, thus staying very close to our estimates. Given the balance of the current risks, we keep our GDP forecast for 2022 at -33%.

Disclaimer 3

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Preliminary data on GDP dynamics over the second quarter came out unexpectedly and with more than one month delay. In fact, the data just clearly reflected **the primary reaction of the economy to the war shock**. The war had also put its harsh mark on the promptness and the degree of statistical data. We still have **no assessments** from the State statistics office **on the detailed dynamic of GDP** for the first quarter by its main components. However, under current circumstances and due to the lack of data, publishing just GDP dynamics remains an extremely important indicator by allowing us to compare it with our estimates and forecasts.

The drop in real GDP in the second quarter of 2022 hit a record of 37.2% yoy, thus staying **very close to the figures we projected**. However, we were slightly more pessimistic vs actual data by forecasting a drop of 40% yoy over the period. Therefore, the actual figure on the record decline in real GDP in the second quarter and our outlook for the remaining two quarters of 2022 provides us **with the possibility for a potential upward adjustment in our whole-year forecasts**. In qoq terms, the GDP recorded a 19.1% drop over the second quarter of the year, thus indicating the technical recession and pointing to the fact that 1Q22 GDP data still reflected a portion of the economic dynamic in the pre-war period. We still consider **April as the worst month in the second quarter** in terms of economic activity. Also, we estimate a gradual recovery in business activity began since then, which was backed primarily by the release of territories in the north of Ukraine and by improving business and consumer expectations, tax revenues and other indirect indicators of business activity.

In terms of components, we still believe that **business took the main burden of the war**, which could result in a **drop in investments by around 70% yoy** over the second quarter. On the contrary, the main component of GDP, i.e. consumer spending, is expected to be halved over the period. At the same time, state programs to help the population (especially the displaced people) could mitigate the sharp drop in disposable income, thus smoothing the potential negative dynamic in consumption. We still estimate the contribution of government purchases and net exports as relatively insignificant but

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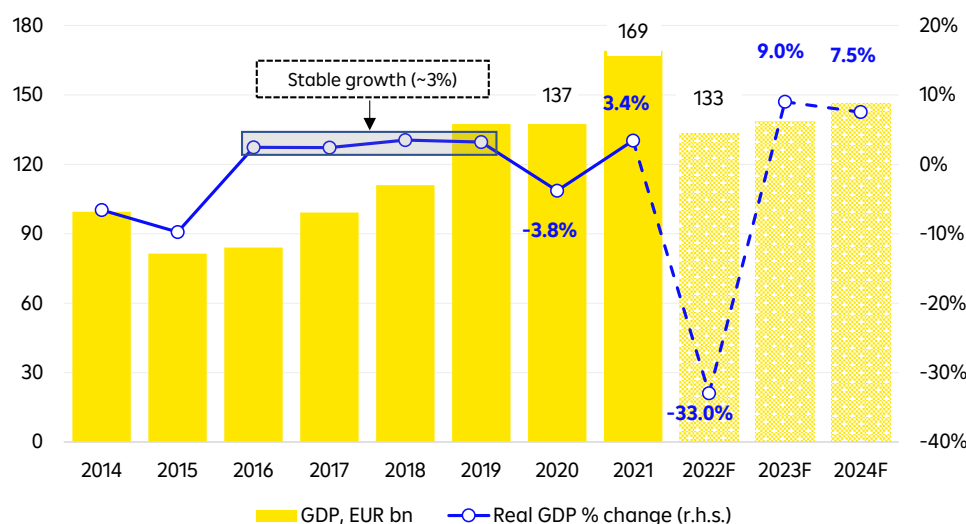
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negative. We believe **the negative trends in private consumption and investment will continue until the end of 2022**, albeit somewhat milder than in the second quarter. Indeed, a solid package of external financing allowed to raise budget expenditures substantially in the summer months, thus supporting government consumption and, indirectly, consumer expenditures. Also, gradual improvement in external trade after the initiation of the grain corridor should somewhat improve the net exports' dynamic.

**Chart 1 - GDP growth and nominal GDP**



Source: Ukrstat, RBI/Raiffeisen Research

We believe **the GDP dynamic over the second quarter of this year should be the worst-case figure** as, according to our estimates, the domestic economy in the second quarter faced the most dramatic negative impact from the war. This is also clearly seen in the reaching of local minimums by both business and consumer confidence indices in June. We also see clear signs of accommodation and cautious recovery of the economy from April onwards. This is additionally reflected in the gradual recovery of market sentiments recently. Therefore, according to our estimates, **GDP dynamics in Q3 and Q4 will be slightly better than the Q2 figure**. We thus **stick to our April forecast of a 33% yoy fall in real GDP in 2022**, although, in contrast to previous estimates, the balance of risks has shifted towards an improved outlook. At the same time, significant uncertainty and negative risks associated with the war remain very high, and many positive trends, particularly enhanced logistical opportunities for exports, are pretty fragile.

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
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