

UKRAINE: STRANGE ECONOMY AT STRANGE WAR

Author: Bohdan Rybka

UVA2D1

Ieva Bruksle

Faculty of business administration

Department of commerce

Turiba University

Introduction

Ukraine long time lives in peace and harmony. The same was with Ukrainian economic system and economy in general. But when the terrible things happened people of Ukraine can't be behind it. Also we can say it for economy. When a war comes in home you should protect it from aggression and occupation. You should use all methods to protect your relatives, friends, people which around you. In a way of war economy is extremely important. But in Ukraine we can see a lot of differences in economy for satisfy needs for army.

The main idea that Ukraine didn't change economy system from simple market or capitalistic way to war way. But first of all we should measure Ukraine real situation and opportunity for development. I found this real situation quite interesting for all types of economic theory. Also that situation in Ukraine will be quite interesting for marketing research, because situation in Ukraine change every day and needs of market also change.

Research aim and tasks

The course paper tries:

- 1.To measure Ukrainian real economy situation*
- 2.To find loses and opportunities*
- 3.To find and influence of war to Ukrainian economy*
- 4.To find identify needs of market and problems of marketing development.*
- 4.To make a conclusion with using real resources and calculation*

1 Economy pre-war situation and Ukrainian losses

1.1 Pre-war economy situation in Ukraine

In March 2014, when Yanukovich ran away from Ukraine, the government began to control new power which was formed from opposition. I am a member of one party from opposition and I can operate with real numbers. So after Yanukovich moved out from Ukraine he left for Ukraine 11,5 million UAH which was approximately 1,2 million USD. It was a very big problem. The first move was to use Ukraine gold reserve for amount of two billion USD. Next step was printing a new UAH for amount of 30 bln UAH (NBU, 2015). Of course these steps led to UAH value collapse. UAH fallen from 10,5 for dollar to 14,6 for dollar. It was a first signal that Ukraine economy begins to fall. Next problem was commodity turnover with Russia. When Russia began to occupy Crimea some of Ukraine companies stop trade relation with Russia for reasons of blockade (Russian and Ukraine) or for principle. The main problem is that Ukraine has 34,8 % (Head, 2014) of export directly sells to Russia. It was a biggest Ukraine trade partner. Blockade of Russian trade for Ukraine also had very big influence. Ukraine product was blocked in border, Russian product nobody be able to buy. Entrepreneurs lost their money, Ukraine also lost them. Another problem its gas and oil. Nearly 30 percent of imports to Ukraine from Russia are gas, oil and products of its distillation. With blockade of products and goods began an energy blockade of Ukraine. Russia used to put price for energy rather hi than Europe countries. This is due to Russian undesirability to release sphere of influence on Ukraine.

After Crimea occupation Ukraine government faced with hole in budget and finances. They weren't ready for occupation. Ukraine bureaucracy slowed down a realization that Crimea is under occupation. This situation changed after president election on 25 of May, after two month of occupation. In that time Ukraine begun to war with Russian collaborationists and separatists. Ukraine lost great industrial capacity. UAH fell down with more power with hitting new records. Problem of lack of money in the budget not engaged entrepreneurs and economists but a printing machine. Ukraine energy problem had a solution to buy it from Europe, because it was way cheaper to buy it from Poland, Slovakia and Germany. But Russia began to use their influence and threats in Europe to block this types of deals. Also economy situation was complicated absence of real reforms both economic and political. Lack of real support from EU. Pause the association and of its economic part totally stopped development of entrepreneurship. The absence of strong character of Ukrainian government, lack of volitional decisions and real reforms, absence of clear solution about the way of Ukrainian economy lead to significant losses – economic, social, people losses.

1.2 Ukrainian loses

At the beginning for find solution and opportunities we should measure Ukrainian loses. What did Ukraine lose and what will lose tomorrow? For answer this question we should analyze Ukraine pre-war statistic and calculated it in real numbers.

1.2.1 Economical regions of Ukraine

Black-Sea-Costal. The structure of the Black Sea Economic Region includes the Nikolayev, Odessa , Kherson and Crimea . Area - 113.4 km². , In the Kerch peninsula lies 2.8 billion tons (14 % of reserves Ukraine) iron ore. Also we had discovered oil and gas fields on the Kerch peninsula, Crimea. The share of the chemical industry is 20.6% of the total industrial production of the republic. There are the largest chemical companies in Crimea that act as monopolists in Ukraine and CIS. They are produce unique and competitive chemical products in the European and world markets. The key enterprises of the industry (93.7%) located in North Crimean region. They are SSC "Titan" and JSC "Crimean Soda Plant". Ukraine lost 14% of iron ore , opportunity for energy independence , tourist mecca post-Soviet states . From the beginning of 2009 Ukraine begun to spend a lot of money to develop natural gas and oil field on Black Sea shelf. The amount of cost was 20 billion USD includes exploration, purchase of machinery and tools, delivery and installation of gas stations. Ukraine also spent considerable sums of money for the construction of oil and gas refineries. Today all of these industry is captured by Gazprom. But still we must note that in 1991 Ukraine had annual costs for infrastructure Crimea, social needs, bureaucracy, and construction which can be estimated in the hundreds billions of UAH. Also Ukraine had a biggest port in Europe in Sevastopol. But despite all the advantages Crimea is budget hole of Ukraine. For all history from 1954 Crimea didn't earn money for Ukraine. For example statistic about budget transaction for autonomy republic Crimea in second quarter of 2013 was:

- a) Transferred into State Budget – 1, 94 bill UAH
- b) Received from State Budget – 5,72 bill UAH
- c) Surplus / deficit - -3,78 bill UAH (Golovaty, 2014)

As we can see Crimea doesn't make any profit in Ukraine, but Ukraine tried to make opportunity to develop that in region in very strong economical part of Ukraine. That try was stolen

Donetsk economic region covers an area of 53.3 thousand km² or 8.8 % of Ukraine with a population of 6.67 million people. It is consists of Donetsk and Lugansk regions. Within the area is Ukrainian Donbass (a highly TEC with specific extractive industries and replacement processing industry). Typical is a powerful production capability. The main wealth of the subsoil Donetsk economic region is coal (from long absorbing to anthracite). Stone coal seams thin thickness of 40-70 cm in the area of natural gas deposits found in Chervonokopivsku ,

Slavyanoserbksk , Borowski, Spivakivskomu , Kruzhylivskomu . There are 21 gas perspective area . In the basin of Kalmius (Donetsk region) and Aydar and Derkul (Luhansk Oblast) found hematite's nonindustrial field value. The region has reserves of these minerals: salt, limestone, chalk high quality, refractory clay and cement marl. Runs 21 production association of coal that include 214 mines. Also in the region there are complex of Mining Company and coke production. Powerful chemical company is located in Ukraine in Severodonetsk. Also like Crimea Donbas region is a key for Ukrainian energy independence.



Fig 1.1 Sloviansk is a centre of deposits of shale gas

From this picture (Fig 1.1) you can see a deposit of shale gas and its center – Sloviansk city. This city was first which was occupied by pro-russian separatists. So the main point is State Service of Geology and Mineral Resources of Ukraine estimates inferred reserves of traditional and unconventional gas in Yuzovsky bearing area of 7 trillion cubic meters. Also Ukraine make a deal with company Shell for exploration and production gas in that region. According to the Interdepartmental Commission of the conclusion and implementation of PSA, industrial extraction of shale gas Yuzovsky area should start in 2018-2019 years. But the war is come. And first strike was a center of gas independents – Sloviansk. In march of 2015 Shell company rejected contract with Ukraine for using this resources. With gas Ukraine lost coal. There are more than half of all miseries in Donbas was under separatist control. At the beginning of winter of 2014-15 Ukraine had a lack of energy because of lack of coal. Mostly all cities went to economy way of using electricity. For example in Poltava electricity was switched off for 6 hours which was divided for day. Ukraine also lost a lot of very big strategic plants and factories for producing ammunition and armory, metal factories and machine plants. But as the same as Crimea Donbass region is also take more money than give. In total Donetsk and Luhansk regions had:

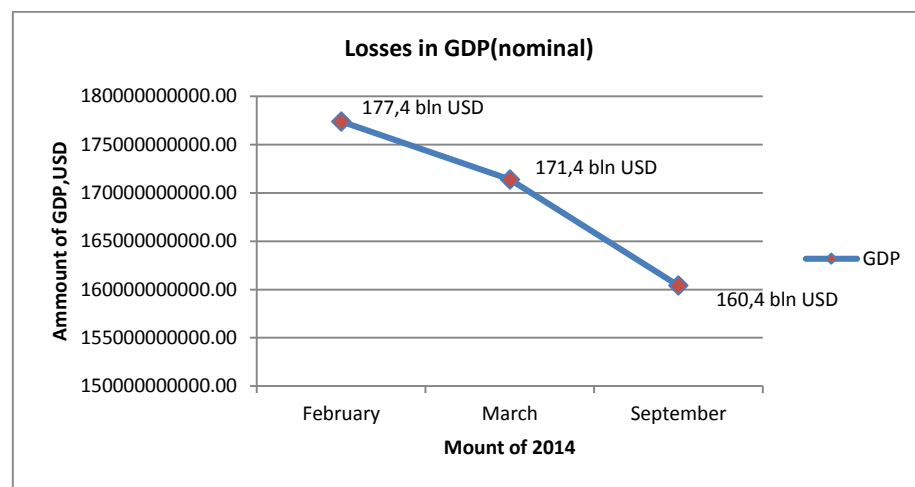
- a) Transferred into State Budget – 8,2 bill UAH
- b) Received from State Budget – 22,51 bill UAH

c) Surplus / deficit - -14,31 bill UAH (Golovaty, 2014)

So as you can see that Donbass region is donation region of Ukraine. That happened because of population and their social payments, donation for miners (in Ukraine is unprofitable charcoal miners), support of major medical centers (Ukraine build unique hospitals and medical centers there).

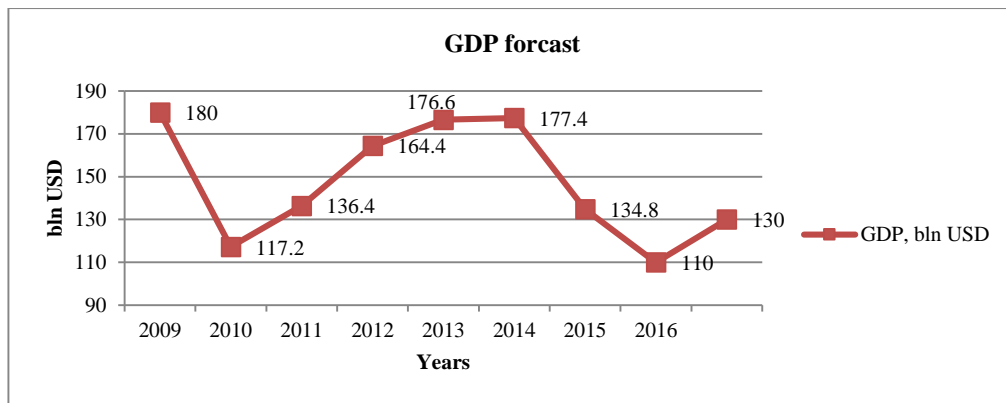
1.2.2 Loss of GDP

At the beginning of 2014 GDP of Ukraine was \$177,4 billion. If we calculated it for capita it will be \$3900, 47. With using analysis of Ukrainian population (with numbers from CVK) we can calculate Ukrainian losses for GDP depend on population which occupied or in war. We begin with Crimea. In information of CVK we can find that population of Crimea which could be calculated in GDP are 1541052 peoples. If we multiply it with GDP per capita we will find losses for GDP with Russian occupation of Crime. It will be 6 010 827 094,44 USD. Calculation for Donetsk region. There are 1845234 of Ukraine population now under occupation. We can calculate it in same way. So Ukraine losses in Donetsk region are 7 197 279 859,98 USD. Calculation for Luhansk region. Population which occupied – 967895. Losses in GDP (using same calculation) - 3 775 245 410,65 USD. Total losses of GDP by using per capita calculation methods - 16 983 352 365, 07 USD.

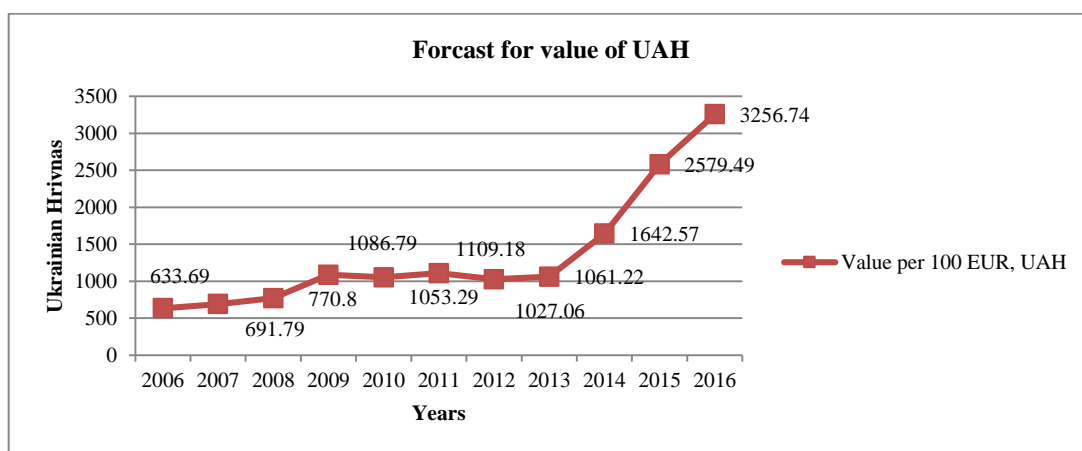


Tab 1-1 Losses in GDP after critic month (Population of people from 18 years, 2013)

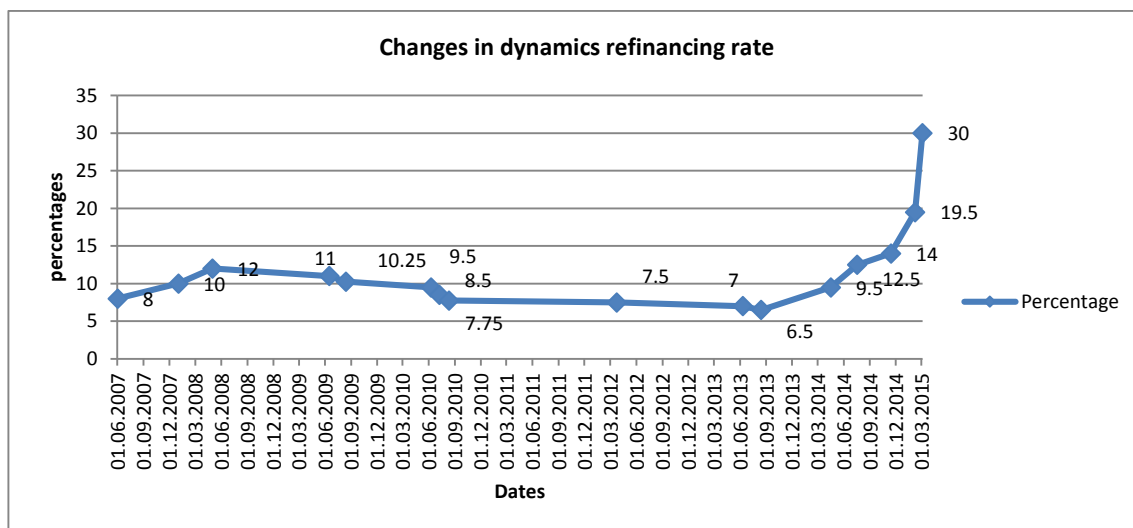
And it was just very rough calculation includes only population factor. The real forecast will much less because it will include losses in manufacturing and industrial potential, a decline of the hryvnia. Also we should include that in Ukraine for this time a lot of companies are going to close. At the beginning of 2014 the amount of entrepreneurship was 1722070 includes enterprises and individual merchants. With occupation Ukraine lost 77529 economic units from Crimea and 124196 units from Donbass economic region. So all these factors also influence to the nominal GDP of Ukraine.



Tab 1-2 GDP forecast for Ukraine



Tab 1-3 Forecast for value of UAH



Tab 1-4 Changes in dynamics refinancing rate (Rates, 2015)

1.2.3 PEST analysis of Ukraine

P – Political factors. So first of all Ukrainian political factors are negative, because of war. But I can say about stability in government and administration of president. All elections are past and Ukraine doesn't need to spend extra money for new elections. Also Ukraine waiting

for ratification of association agreement with EU which will stimulate Ukrainian export and import. Also Association guaranteed changes in legislation, which will be more interesting for investors. Ukraine have membership in WTO and GUAM. The main negative factor is war, this factor scared many investors from Ukraine. Another negative factor is tax law which is the worst index in the world (International Finance Corporation). The main problem which I can't understand its absence of real reforms and changes.

E-Economical. About dynamics of GDP you can find information from Tab 1-1 and Tab 1-2. You can see that Ukrainian economy going through hard times. Ukraine inflation rate is 272%(Ukraine's Hyperinflation Rate Boosts,G.Samman). SO we can speak about hyperinflation now in Ukraine. You can see forecast for value of UAH from Tab 1-3. About refinancing rate you can see from Tab 1-4, also quite negative rate which shows problems in Ukraine banking sector. The amount of officially unemployed economical active person are 523,1 thousands, its 8,9% from total amount of people from 15-70 years (Rates, 2015) . It's a good indicator if we compare with other counties. About Ukrainian market basket I can say that its smaller than other European countries. There are 297 products in In Ukrainian market basket, 65% of them its food , other for service and other products. (Ukrainian purchasig power and busket, 2014)Minimum salary is approximately 53 Euros (rada, 2014)Ukraine has worst taxation system in a world. You should spend 277 hours per year for pay Ukrainian tax , also you would give 57,1% from all your economic activity (Ukraine analysis , 2014)Ukrainian purchasing power is in defilation, because of changing value of money and increasing of prices and no increase in wages and salaries. Active part of Ukrainian expenses takes military expenses. Ukraine search an opportunity to buy European or American weapon because its different with Russian and make some tactical advantages.

S-social. Ukrainian society are more patriotic today. Ukrainians begin to purchase more Ukrainian production and goods. Today in Ukraine its mostly forbidden to buy Russian production , so it's quite bad for people who realize this product in Ukraine . If Ukrainian need to change form Russian production to other so he purchase Ukrainian and European(if there is no Ukrainian variant r quality is terrible). Today in Ukraine the most popular articles for personal care because the market was almost monopolized by Russian manufacturers. Ukrainian market was always open for The European luxury goods. About demographical changes I wrote in part about loses of GDP. Ukraine lose quite important market – Crimea , the tourism center of Ukraine. Mass media is very strong power in the Ukrainian society today. In the environment of hybrid war media taxes vary big part, so a lot of people invest in media and makes new types of media like public media were all people are investors or big Ukrainian canals projects also quite

profitable now. Ukraine even make a ministry of information. The main idea is to make ukrainian canals more popular in Ukraine and in the world.

T-technical. SO this part is quite important for European because Ukraine needs of new technologies and this applies to the military and all other areas. For example city transport. Ukraine system of city transport is quite old and Latvian experience in it will be very usable in Ukraine. For making this system of E-talons man who provide it can make very big profit. Also system for making tickets to remove queue. There is no system or machines which same in Ukraine. These are just two examples but Ukraine need tech changes in many sectors.

2 Current situation and opportunities

2.1 Current situation

The Ukraine and Ukrainian economy still live and develop despite all loss. At the beginning of 2015 Ukrainian nominal GDP was \$134.8 billion, so as I wrote before that my calculation wasn't complicated. The fall in value of Hrivna also provoked decrease in GDP. Inflation at the beginning of 2015 was 272%. But Ukraine government doesn't try to change economic environment in Ukraine. The worst tax policy wasn't changed. The situation with bureaucracy and corruption wasn't change as well. There are some new problems which were added to that one. They are lack of resources, paper and administration confusion, failure to sign Association with EU and that economic part. Manufacture of weapons and ammunition takes a big part of Ukrainian expenses. For example. Production of 14 caliber bullet cost 3,2 Euros . When I was in Pesky(village near Donetsk) I saw how three Armored infantry vehicles spend 1500 bullets per day. So if we take most 7 critic point of ATO and have some calculation we have :

- a) 10500 14,5 caliber bullets spend every day
- b) 33600 Euro spend every day to produce bullets for three AIV

So it was just calculation just for 14,5 caliber bullets for three AIV in seven hot points. But imagine how much Ukraine spend with using artillery, tanks, grenades , other bullets , rpgs and supply . It is hundreds of thousand Euros and millions hrivnas every day. Today all heavy armored or big caliber weapon is forbidden to use in ato. But the aggression wasn't stopped. So Ukraine continues to produce ammo. Also we should include a lot of money spend for medicine. Only in military we have more than 5 thousands wounded soldiers and uncalculated amount of civil people.

As I said before our government do nothing to change economic situation. Previous governments tax code wasn't change and this thing make investors run away from Ukraine and businessmen push to close their business. They even make new type of tax which called "War Tax"- it is takes 1,5% from every profit. Lack of money in the budget provoked them to put new taxes and fees into Ukraine economy. Also for the beginning of 2015 National Bank of Ukraine printed 107 bln UAH. This factor is also not good for economy because it influence on value of hrivna. In a general plan of NBU wrote that they should print more than 100 bill UAH for next three years. We are waiting for a new devaluation. Rampant situation is also with the shadow economy. Real percentage is approximately 60 from GDP. Entrepreneurs try to hide profit from taxation using cheating methods which officially legal. Like "GDP squares" which invented by over ex-prime minister – Mykola Azarov. These "GDP squares" helps you to return GDP from

government. Also the biggest problem in Ukraine is corruption. Ukraine government didn't control or fight with it. As same with budget information I can operate with real information from government because three of our party members were ministers. When after the Maidan they came to work in these ministers (Ministry of Agricultural policy and Ministry of Ecology) they said that from this day we stop all corruption operation. For the next day a lot of workers of ministry sabotaged their work because they were not agree with no-corruption regime. The main problem that in Ukraine Civil Code is illegal to fire the person with no reasons and without three prevention. There was a possibility do fired corrupted personal with lustration law , but it was also sabotaged. The main interesting thing from my research of corruption that mostly bribes goes up on hierarchy ladder. For example if inspector of road police or example if inspector of road police take bribe , he will leave 10% to himself and past other 90% to higher officer. That officer also had bribes and with that 90% he should leave 10% for himself and give it up to local head of road policy. This local head repeats same thing and give it to regional head. And this regional head gives it to Ministry of Internal Affairs. Employees of ministry also have same rules. So without this little profit they sabotaged all work. That ministry which tried to stop corruption showed the worst results of work. So the same system is available for all ministries, offices and administrators.

The main problem of today Ukrainian economy is combining both types of economy warlike and market or capitalistic. Ukraine government tried to show people that everything is good but solders and civil people dies every day. Irresponsibility of Ukrainian government stopped opportunities and development of Ukraine.

2.2 Opportunities

Tomorrow of Ukraine is unclear. International rating companies predicting default for Ukraine. But I say that if Ukraine will choose straight way of economy, try to show independence power and strong position that Ukraine will be one of the greatest counties in the world. I can say that today is one of the best time for invest in Ukraine. Ukrainian government will do everything to you if you want to invest in Ukraine economy. But present situation is quite bad for realization foreign product. Because of decreasing value of money, foreign goods can't compete with Ukrainian products. Also fall of purchasing power will influence on selling of foreign products. The best way to invest in Ukraine is invest in production armory and weapon, service activity and agriculture. Also center of Ukraine has a lot of resources which with changes in value of hrvna is quite cheap in extraction and further processing. Today Ukrainian market feels need for new technologies and warmth retaining production for homes, flats and pipes. Market also needed a lot of army supplies. A lot of people now in Ukraine makes

volunteer job for supplying military, and they needed a lot of well quality military , medical or long-term food stuff . Of course the stability in Ukraine depends on conflict resolution, because as I wrote Donbass and Crimea are very important for Ukraine as well as Donbass and Crimea need Ukraine. Further escalation of the conflict will degrade the situation in Ukraine. Of course we should not exclude the possibility of full occupation of Ukraine. But in my opinion full occupation isn't required and hurt the aggressor country both economically and politically. Russia doesn't need 38 million not humble citizens. My prediction that this conflict drags on for two more years. Many people will die, but Ukraine will be united. It is important that the warring parties came to conflict resolution.

References

- Documents discussion* . (2015). Retrieved from Ministry of Economic development and trade of Ukraine :
<http://me.kmu.gov.ua/control/en/>
- Golovatyj, R. (2014, 11 5). *Budget expensess* . Retrieved from Investgazeta.
- government, U. (2010). *Tax code of Ukraine*.
- Head , o. o. (2014). *Ukrainian trade operation*.
- NBU, A. d. (2015). Plan for cash printings . *Ukrgaz*, pp. 14-16.
- Official information* . (2015). Retrieved from National Bank of Ukraine :
<http://www.bank.gov.ua/control/en/index>
- Ovchar, T. (2015). Основна сфера економіки України різко скоротилась. *Ukrainian Economist* , 1-20.
- Pimenov, A. (2014). Creation of Ukrainian federation. *Investmagazine*, 13-40.
- Population of people from 18 years* . (2013). Retrieved from Central vote comitet .
- rada, V. (2014). *Budget expences for 2015-2016*.
- Rates*. (2015). Retrieved from Bank.UA.
- Reciept of the State / Budget of State* . (2015). Retrieved from The Price of the State (Ukraine) :
<http://costua.com/en/>
- The decreasing of ukrainian GDP can mached with trade turnover. (2015). *Ukrainian Economists*.
- Ukraine amalysis* . (2014). Retrieved from International finance corporation:
http://www.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/home
- Ukrainian purchasig power and busket*. (2014). Retrieved from BBC Ukraine.
- Паламарчук М. М., П. О. (2008). Розподіл на Економічні регіони. In П. О. Паламарчук М. М.,
Економічна і соціальна географія України з основами теорії (pp. 90-140).
- Статистична інформація : Кількість суб'єктів господарювання за регіонами у 2013-2014 році*.
(2015). Retrieved from Публікація документів Державної Служби Статистики України:
<http://ukrstat.org/uk>