

Peterson Institute for International Economics

Rebuilding and realignment: Economic future for Ukraine and Russia

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[00:00:21.04] - Jacob Funk Kirkegaard

Well, good morning, good afternoon, uh, good evening, depending on where you are in the world. My name is Jacob Kirkegaard, and I'm a senior fellow at the Peterson Institute for International Economics. And it is a great pleasure for me on behalf of Institute President Adam Posen and our colleagues to welcome you to an economic future of both Ukraine and Russia. I think it's fair to say this is a highly topical event, and it is with great pleasure that I can present what I certainly consider to be an absolutely stellar lineup for you, where we're going to talk about fundamentally two issues. The first is going to be about how we're going to go through an economic transformation in Ukraine that will ensure that it is, you know, in the post— in eventual postwar reconstruction, full realignment with the West to ensure adequate financial flows, investment, and reforms. And then on Russia, where obviously we have an economy that's going through, has gone through full wartime mobilization, dramatic increases in wartime expenditures, and how, what is the resilience level And what is any long-term economic future for Russia also in an eventual post-war situation? And with me, I have a truly stellar panel.

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We're going to start with Professor Yuriy Gorodnichenko, who is the QuantEdge Presidential Chair in Economics. At UC Berkeley. He has a very extensive set of publications which I know are fully available on the internet should you wish to peruse them. I will not delve into them here. Following his presentation, we're going to go to Elina Ribakova, whom I have the pleasure of being a colleague with both in both at the Peterson Institute and at Bruegel in Brussels. But perhaps more relevantly, Elina is also the— excuse me— she's also the director of the International Affairs Program and vice president of foreign policy at the Kyiv School of Economics, and also has a very distinguished career behind her in both as a practitioner, macroeconomist, and academic. And then finally, we're going to go to my colleague Maury Obstfeld, who has arguably the most intimidating title in international economics, being the C. Fred Bergsten Chair, or C. Fred Bergsten Senior Fellow at the Peterson Institute. He's also the Class of 1958 Professor of Economic Emeritus at UC Berkeley, and of course was previously

the Director of the IMF Research Department and a member of the Council of Economic Advisers during the Obama administration.

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Each of the panelists will speak for about 10 minutes. I will then ask a couple of clarifying questions before we open it up for Q&A with the audience. There is a Q&A function. Please type in questions you might have and I will feed them to the panelists. And we can hopefully have a super exciting discussion about this very topical event. But without further ado, therefore, Juri, the floor is yours.

[00:04:18.23] - Yuriy Gorodnichenko

Thanks very much. Thanks very much for having me. I will have brief remarks based on a recent report published by the Peterson Institute that's joint with Elina and also Ilkka Korhonen from the Bank of Finland Institute for Emerging Economies. And this paper, this report, was motivated by, I think, an important puzzle that we all ask about, which is the performance of the Russian economy. And this figure kind of illustrates this puzzle. This black line was the professional forecast for the growth trajectory for the Russian economy just before the Russian full-scale invasion of Ukraine. Then immediately after the invasion, the professional forecasters revised their projections. You see this red line here. And so in a nutshell, when you compare the black line, the pre-war growth trajectory, and post-war, uh, post-invasion growth trajectory, they predicted that Russia is going to have a massive recession and then basically years of stagnation. Instead, what we see is, you know, somewhat qualitatively similar. We had a small recession initially, at reduced. But then we had a period of relatively high growth. And, you know, when you look at 2024, the Russian economy was basically at the level that was projected before the invasion.

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Now, we have some slowdown now, and we want to know if it's something that is transitory or if this is going to be a trend for the Russian economy going forward. Are we going to be still observing a high growth in Russia, or it's going to be some type of stagnation. Now, at some level, rapid growth in Russia is not rocket science. We know that Russia spends a lot of money on its war machine. We see there is a dramatic increase in military spending, and in fact, Russia now spends more on its army and armed forces more generally than ever since the collapse of the Soviet Union. Now, having said this, you know, we have this massive fiscal stimulus, which would obviously raise the growth rate of the economy. We know when we look under the hood and see, you know, where this growth is coming from, it's very clear from some research done

by our colleagues by the Bank of Finland. We see that for the civilian economy, this is dark blue line, you basically have no growth since the beginning of this war. While if you look at the military industrial complex, in Russia, you see that it more than doubled in size.

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Now, the key question then is, okay, so if we have this kind of source of growth in Russia, is it sustainable? Is it supported by efficient allocation of resources? So we're going to run out of steam eventually because we can produce only so many tanks, so many missiles, so many artillery pieces, and so on. And to answer this question, we need to look at how this spending and economic activity are allocated, not only across industries, but also across regions. Because again, hypothetically, this may be sustainable if all of this military spending is allocated to places where you have a lot of spare capacity, a lot of underemployment, a lot of idle capital. And then, you know, if, if capital and the spending more generally goes to this kind of places, then we can have rapid growth in Russia for, you know, quite some time. So what we want to do in this project I wanted to look at this experience, this, you know, military spending, this, this war has affected regional dynamics in Russia. Russia is a huge country, obviously a lot of heterogeneity, and this map is trying to convey the information that the level of income per capita— and by the way, this is on the log scale— is very, very different across.

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You look at Moscow, Saint Petersburg, they're very rich. Some oil-rich regions are also also have high incomes. But then at the same time, you have some very, very poor, poorer places like here in the Caucasus, in the middle of the country, in the Far East. And so the question here is where the military industry is, you know. If it's somewhere here in poor regions, then it's conceivable this extra military spending is basically paying for itself. It can be supported over a long period of time. If it flows to places where you already have a lot of utilization of resources, then at point, you're going to hit capacity constraints. And so instead of economic growth, you're going to see a lot more inflation. So again, hypothetically, what can happen is if you have this wonderful situation, quote unquote wonderful situation in Russia, where you have oil flowing into poor regions, then we have some type of convergence across regions. And also it's going to be a situation where Russia can wage this war for a long time. Now, where is military production? It turns out to be fairly concentrated. There is a lot of production in the Central Federal District.

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There is something in the Urals, something in the Volga, but, you know, many places don't really have a lot of military production. And so this is telling us that this match between where

resources are flowing and where the production is and where we have poverty is— this correlation is not perfect. And so this is an empirical question then, you know, do we see some type of convergence in income that is fueled by this military spending or not? Now, when you look at this using a sort of standard approach in economics, you have in this scatterplot initial level of income just before the invasion. This is the growth rate of income since the invasion. You see a clear negative relationship here. This is telling us that the poor grew much faster than regions that were relatively well off, right? So this will be consistent with the idea that somehow this war money is flowing into places that are, you know, relatively poor, and this is what sort of stimulates economic growth in Russia. This is where we have a lot of spare capacity. So just, you know, at face value, when I look at this kind of scatter plot, you should conclude that there is, you know, some convergence across regions, which would be consistent with the idea that military spending, this huge fiscal stimulus, fuels economic growth by utilizing resources in relatively poorer places.

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But to appreciate the significance of this, I think it's useful to look at the time series of cross-sectional dispersion of incomes in Russia. So what this plot here shows is the time series of the standard deviation over time, right? So you pick a month and then you say, you know, what is the average wages in Moscow, in Voronezh, in Yakutia, in other places. You calculate standard deviation of this and you do this for every month, maybe smooth the series a little bit, and you're going to see this time series here. Now what you should see here is that when Russia was kind of moving more and more towards market economy, this dispersion in regional incomes was shrinking. That would be consistent with an improvement of allocation of resources. You know, if you really believe in, you know, perfect allocation of resources, then we should see that the dispersion of incomes should be basically zero. So this trend towards smaller and smaller dispersion is consistent with an improvement of resource allocation. Then we have the annexation of Crimea and incursion in the Donbas. This is first vertical line. And we see basically stagnation in this time series.

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There is no convergence of incomes. Why is that? Well, it may be because Russia lost access to international capital markets to a great extent. Maybe the technological transfer got a lot harder for Russian firms. You know, there are many reasons why maybe something like this may be happening. But then we have the full-scale invasion, and we start to see again area convergence in regional incomes. So there is something very unusual happening in the Russian economy. Now, how do we have this convergence? Is this the left tail moving towards the middle, or this is upper tail kind of converging from above towards the middle? One way to

answer this question is to look at the dynamics of differences between various percentiles. For example, 90th percentile minus 10th percentile. Rich regions minus poor regions. We see that this blue line is shrinking, which is telling us that the poor regions are catching up to the high-income regions. This green line is comparing kind of middle-income regions— think about places like Varonish— and some very poor places like Tiwa. And we see that this in here is relatively flat, and this is telling us that this left tail and the middle of the distribution are kind of moving together.

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And then this final scene here, the difference between high-income regions and middle-income regions is also kind of shrinking over time, which is telling us that, you know, roughly speaking, Moscow is staying stable, but then places like Voronezh and Tula are catching up to Moscow. Somewhat an unusual form of convergence, but it's telling us that some resources are flowing to poorer regions. And some of this is definitely, we know from other sources and from our own research, that This is fueled by military spending and, you know, lots of other war-related expenses. Another way to look at this convergence is to see if employment rates are converging across regions over time. And again, we see some trend where we have more and more similar employment rates. Then this trend was dashed by the COVID crisis, and then again with the full-scale invasion, we see more convergence there. Right. So again, saying that in the labor markets, there is a lot of action happening in Russia, which is pointing towards more convergence. And this means that in principle, this can be sustainable in the longer run. However, to really support something like this in the long run, you have to match convergence not only in incomes, but also in investment.

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Right. So this wage growth has to, has to be supported by capital injections, capital inflows. And here the picture is very different. Again, before the illegal annexation of Crimea, we have some downward trend, which is saying that capital is allocated more and more similar across regions in Russia. Then we have Crimea, a big jump, a lot of gains that we did here over the years were completely offset, years of stagnation. And then we have another rapid increase in the, in the cross-sectional dispersion of investment rates. So this is telling us that whatever we see in terms of labor income convergence, this is not really something that can be sustained over a longer period of time because resources are flowing to these places. We have demand-driven convergence, but it is not supported by adjustments on the supply side. And so this is telling us that you can push this kind of convergence only to some extent, and then at some point the Russian economy is going to run out of steam by, you know, from exploiting this. Demand-

driven growth. So when we look at, you know, what we see across regions, we basically have 4 groups of geographical units.

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One is, you know, somebody who is very negatively affected by the war. You know, think about Kursk, an oblast which is very close to Ukraine, and there was a lot of military action going on there. Some places are very far from contact lines, so they're not very much affected by the war directly, but they benefit quite a lot from military spending. Think about Chelyabinsk, you know, the place where you have a lot of, you know, military-industrial complex firms, like, you know, building of tanks and so on. Some places don't really have a ton of industry, but they benefit through mobilization just because they send so many people to the war. They have a lot of injection of federal money into these places, and this is why incomes are growing.. And then the residual category is basically regions which are affected by, you know, forces like this but to a different degree, and so there is some variation there. Now, to conclude very quickly, you know, usually wars are associated with kind of divergence of incomes and everything within countries. We see perhaps paradoxically that there is quite a bit of convergence in labor income in Russia, much less so in terms of investment.

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But we know that this kind of spending, if it's all demand-driven, this is not something that is sustainable, uh, in the longer run. And maybe this is one of the reasons why we see a slowdown in the growth rate of the Russian economy, right? So you kind of exhaust these easy gains, uh, initially by utilizing the resources in relatively poorer places, but at some point they're going to complete this process and you have no more resources resources to be utilized. So in a nutshell, what we say is that, you know, what we saw in Russia in 2023, 2024, uh, was basically demand-driven. There was some gain from utilizing resources more efficiently, perhaps, but this is not something sustainable. Now, whether this is going to be true in the long run or not, this remains to be seen. But, you know, the earliest signs of stagnation would be consistent with our conclusion that whatever Russia had in the previous years since the full-scale invasion is not really sustainable. So I'll stop here and thank you again.

[00:18:38.02] - Jacob Funk Kirkegaard

Well, thank you very much, Yuriy. Extremely interesting. Elina, without further ado, over to you.

[00:18:45.18] - Elina Ribakova

Thank you so much. And it's a great pleasure to be here with my colleagues. Yuriy talked a lot about Russia and Russian economy and outlook, and Maury will then talk about outlook for Ukraine. Also, this paper was Yuriy. So I will try to provide a bridge. I don't have a presentation and I will just try to focus on maybe giving you an overview of the current state of affairs, then talk a little bit about why Ukraine has managed to hold out for this long, the role of the allies, and also what finally to sum up it means for Europe. So if you think about it 4 years back, you know, about current events, we're discussing a potential for a peace agreement, however elusive that might be. But if you think about 4 years back, Russia was expecting a quick victory in 2022. And I dare say it was not only Russia that was expecting this quick victory. Very often we hear about relative size of the countries, GDP of one country, another, labor in one country, another. And then many people reached quick conclusions that Russia should be able to have to proclaim this victory relatively quickly.

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Yet 4 years on, Ukraine is still standing and pushing back Russia's aggression. As of now, probably Russia controls roughly 19% of Ukraine, including the pre-2022 occupied areas. And in 2025, Russia possibly gained maybe 3,000 square kilometers. Russian authorities themselves claim more, 5,000, but there are a lot of debates. So let's sort of split it in the middle somewhere. But nobody would argue that these gains are scattered, strategically limited, and costly. And that's why we're having sort of Russia put pressure, including within the US-led so-called peace plan, for Ukraine to surrender territory which is heavily fortified and which Russia has not been able to take over. And I think that's, I'm very happy that recently even sort of the New York Times, I think, and others have been writing more in an accessible way explaining why exactly this sort of Russia's reach for territories that they couldn't conquer, why are they trying to use and dress it up as a peace agreement? Well, at the same time, Ukraine has put forward a message for a while now that they would welcome unconditional ceasefire according to the current line of contact and then would be able to start the negotiations.

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So the big question is why Russia has not been as successful at putting its overwhelming advantage of size to a better use, right? So I think the first and foremost is that Russia's structural weaknesses. We've had long-term monopolies, limited private initiative, and weak value chains, low value added of production, and also high dependence on Western-made components made Russia vulnerable to pressure of the sanctions and also unable to project power in a way that it was planning to. As Yuriy has explained very well, there's been a cyclical upturn thanks to spending, military spending in the budget, but it's not something that has led to investment and definitely not productivity spillovers to the civilian economy. Then we've also

had Russia's allies have been much more limited and maybe somewhat less natural, dare I say. If you think about the typical gravity model, Russian economy and even a lot of the resources are still concentrated in the European part of the country with much more natural transportation links to continue to work together with Europe. Yes, a closer relationship to China is warranted because they do share a big border and they have large populations and large GDPs.

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So, you know, some acceleration in that approach, cooperation is warranted, but not a pivot fully away from Europe into China. At the same time, and Maury will talk much more about Ukraine, I think people, many of us on this call as well, who've looked at Ukraine for more than 20 years, many of us maybe sometimes remember the pre-2014 Ukraine. The Ukraine now is extremely different. Major reforms took place since 2014. And if you were to have this kind of invasion in 2014, it would've been very difficult for Ukraine to hold back because the war, or rather to hold back their territory rather, because the war is not just about the military action, it is also a massive macroeconomic shock, economic resilience. So if you look, we are very quickly oftentimes to point out mistakes in the reforms, but also let's look at what actually was done on the plus side, on the positive side. So if you look what has happened since 2014, we've had completely revamped National Bank of Ukraine. So they used to have all kinds of inappropriate assets, you know, had very sort of much less qualified personnel. It was forever the cycle of fixed exchange rate regimes and then maybe debt in foreign exchange.

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So all of these classical problems of emerging markets. So since then, Ukrainian authorities went for full inflation targeting before the war. They've cleaned up the banking system despite pressure from the politically connected oligarchs. And they've also divested non-core assets of the National Bank of Ukraine. So thanks to that, the National Bank of Ukraine could maintain financial sector stability. And even that we've seen some credit growth and some stabilization in the exchange rate and stabilization of foreign exchange outflows even this year because of this pre-preparedness or pre-done homework before the war. So this is on the National Bank of Ukraine. If you think about the fiscal reforms, Just to highlight a couple of them, decentralization was a very important reform which allowed more responsibilities to the local authorities in Ukraine and also bigger ownership of the way they spend money and their accountability. That was a very important reform. Prozorro, many are familiar with that name. You know, it is sort of transparent procurement system which allows you to track in great detail how the government contracts happen and also how the bidding happens, what are the prices. And if anything, one could say that Europe We could use that as a lesson now that we're thinking about the common procurement for the military.

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It could be one of the sort of examples how to create this very transparent digital procurement system. Then we can also talk about the tax improvements and other measures. And then of course, let's not forget the anti-corruption reform. That's where the international donor community oftentimes had the difficult relationships in terms of how people are appointed on the boards, how the national anti-corruption bodies, NABU and SABO, staffed and how do they function and how they work. But a lot of progress has been made. But I think here the most important progress or even consistency is the total civil society engagement. And most recently what we have seen in the summer when the president's administration tried to, president's office tried to curb some of the responsibility of these institutions in the summer, people actually came out on the streets. So there was a very sort of groundswell resistance to these measures. And eventually we have seen, you know, the most recent events where some people had to step down from the administration. And let's see how this situation develops. But to me, it's an important signal that there is this total civil society engagement on one hand, and on the other hand, that maybe these organizations are finally being able to reach for the highest levels of power to be able to tackle or ask ask inconvenient questions about corruption.

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So a lot remains to be done, but let's not forget that also a lot has been done since 2014. And then finally, of course, not last but not least, is the innovation and the military effectiveness. Some could say that this innovation happens maybe not always thanks to the institutional structure, but maybe despite institutional structure. But nonetheless, there are these creative solutions, for example, where each brigade can buy independently their military equipment. They have a common marketplace, but they have standardized procedures or standardized criteria for what they can buy. But at the same time, they can go as if to a marketplace and decide what they need and why they need it and how they can go and purchase it. There isn't always the centralized procurement that comes from the top, but instead, these brigades can work as almost independent businesses, making sure that they procure what they need. And for example, again, this model, Could be something that's used for Europe, for individual member states, where each member state, of course, we would like to have domestic production and domestic drones, but maybe we could go for a centralized standard and then we fit into that from sometimes national procurement.

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And then the very important sort of the last, but the very last, but not the least is the current discussion in Europe. So we started with the discussion with the relative sizes of the two economies, the fact that Russia was not successful at leveraging their firepower to be able to squish Ukraine in a matter of weeks. Ukraine managed to do a lot of reforms since 2014 to be able to resist Russia's war of aggression. But of course, the critical sort of final tip on the scale was financing and support and innovation also from the Western partners, especially from Europe at the moment, now that US is stepping back. So here, of course, the discussion, and I'm sure it will come up in the questions, The discussion about Russian reserve assets is a critical one because relatively small share of Europe's GDP, this is less than 1%age point of GDP. And it's also money that Russia should in theory pay for something that, you know, as reparations that could go a long way towards protecting Europe itself and not just Ukraine. As you know, the IMF estimates the fiscal gap of about \$65 billion for the 4 years.

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A lot of it is concentrated in the coming 2 years. In addition to that, military spending probably needs to increase by another \$65 or so billion per year, which is significant spending. But if you look in the context of European spending on the military, and Yuriy was just showing the figure, it's a very small price to pay for the defense of the whole Europe. So with that, I will pass it on to Maury, who will talk about the future of Ukraine in the peacetime and not only. Thank you.

[00:29:24.10] - Jacob Funk Kirkegaard

The floor is yours, Maury.

[00:29:28.09] - Maurice Obstfeld

Okay, thank you, Jacob. Let me share my screen. And I'm going to go back to where Where it begins, sorry. Yeah, this is a joint paper with Yuriy. We wrote it for the new CEPR publication, Economic Policy: Papers on European and Global Issues. An early version is on their site and a fact-checked version will be issued in a matter of weeks by the Peterson Institute. I'll explain at the end why we, we call this You Only Live Twice. So one can discern four epochs of modern Ukrainian history. First is the period right after the transition from the Soviet bloc. And as you can see here, at that time, Ukraine in terms of per capita income was a fairly prosperous country relative to peers in the Soviet system. But it underwent a total collapse, incredibly high inflation, hyperinflation afterwards. And this process, you know, bottomed out in the late 1990s, around the time of the Russian crisis. Uh, epic two— epic two is a recovery, uh, period with currency reform, but, uh, inflation still quite, quite volatile. But GDP per capita did, did nearly double, as in many other emerging markets. Our global buoyancy in emerging markets around the world, uh,

Epic 3 is the period after the global financial crisis, where in common with, with many other countries, but perhaps more so than many emerging markets, Ukraine stagnated in the face of weak foreign demand, continuing corruption, and domestic political infighting, all of which held back growth.

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And finally, uh, epoch 4 began with the Russian aggression in, uh, in 2014, the illegal annexation of Crimea, the incursions in the Donbas. And as, as Alina mentioned, uh, this, this was a period of, of policy progress in many respects, but it was also a period that was challenging for, uh, for growth. Um, uh, then came the Russian aggression in, uh, uh, the year, uh, 2022, and this had a devastating effect on the economy, with, um, the unemployment rate, uh, down up 30%, uh, uh, uh, uh, with 9 million Ukrainian refugees. And, you know, we all know the, uh, the story. Epoch 5 is the post-war period, and that will be to come. It may come sooner or later. We hope sooner, but this will require a transition to a peacetime economy, extensive rebuilding, overcoming long-term structural challenges, and joining the European Union, the, the Ukraine received candidate status for the EU in June 2022, and, uh, 2 years later, uh, it began accession talks. Um, uh, what will happen with NATO is a matter of some contention, obviously. So what we ask in the paper are some key questions. Uh, first of all, what are the main engines of economic growth?

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How have those evolved? We look at population, productivity, and capital, and what can we do to accelerate convergence to EU peers. And the central message of our analysis is that Ukraine needs massive investment. Um, let's look at the population. Uh, um, there's broadly, uh, based depopulation in Eastern Europe, particularly in war-affected countries, but it's been, it's been quite, um notable in Ukraine. Uh, productivity growth has been slow. Uh, a number of countries have caught up impressively— Poland, Czechia— but Ukraine has stagnated since the global financial crisis. And finally, while Ukraine was reasonably capital abundant at the time of its exit from the Soviet bloc, Ukraine has lost in capital intensity. Growth accounting exercises show that dramatic capital deepening has played a key role in countries in Eastern Europe which have had growth miracles. Where did the capital come from? This chart indicates for countries that eventually joined the EU, it's been largely a function of FDI. Poorer countries have relied more heavily on remittances. FDI is particularly important because it's positively correlated with private investment. Now, of course, there's reverse causality here, but it's a kind of a virtuous circle. Where more foreign investment creates an environment favorable for domestic investment and vice versa.

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And you can see that clearly in the left-hand chart. An empirical analysis in our paper indicates that for Eastern European countries generally, a key element in the rise in FDI has been EU or NATO accession, and we provide some impulse response functions here. But even the start of negotiations for these has had an important positive effect. Um, how much capital will Ukraine need? We look at a period of about 10 years, and first we ask, what, what would Ukraine need just to rebuild lost capital. Our estimate is about \$20 billion per year over 10 years. Uh, but we would also want Ukraine to stop falling behind its peers such as Poland, and that would require an additional \$10 billion a year, and to deepen, uh, the capital-labor ratio, uh, further and induce modest convergence, probably another 10 billion a year would be needed for a 40 billion per year total. We think this is entirely doable. Poland's net FDI was a 20 billion inflow in 2024, and Ukraine has been receiving extensive budgetary support, uh, uh, during the recent period. There are also EU resources for much of which, or some of which at least, could come to Ukraine.

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And finally, as Alina mentioned, it's absolutely critical to mobilize the frozen Russian assets, and we hope that will happen in the, uh, the coming days. Ukraine also faces a debt overhang problem. Overall public debt is roughly 100% of GDP right now. If you look at its breakdown, there is certainly some debt to external private creditors. Eurobonds were extensively restructured in 2024, just in the past days. Ukraine reached an agreement with the private holders of GDP warrants issued in connection with the 2015 restructuring. But the big item here is really the debt to external official creditors. And this is going to require a deep restructuring according to the IMF for this level of indebtedness on the part of the government to be sustainable over time. Ukraine will also have to receive sizable grants, probably to support our inflow. And a part of our paper, which I'm not here, indicates that there could be policies to bolster domestic saving, domestic investment, on the fiscal side, because there are a number of extra— which suggests that having more capital yields benefits beyond what the market perceives. One example is the idea that if you have more capital, you have a higher marginal product of capital— of labor, you have a higher wage, and then you can induce some of the diaspora labor force to return, and that would be a positive for growth and for debt sustainability.

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Some caveats: any tax policies that you have to induce investment and limit consumption must protect the most vulnerable. But you do want to limit consumption, not only to spur investment, but to prevent real currency appreciation, which has been the Achilles heel of many stabilization programs. Ukraine's absorptive capacity can probably manage all of this, but again, many of the

past reforms that Alena discussed, including in procurement, are important for this. And though in allocation efficiency, for example, more privatization maybe setting up a reconstruction agency to efficiently use resources. And as we said, say, in the paper and argue strongly, domestic saving will have to be mobilized both for the short-run reconstruction efforts over a decade, but also for longer-term prosperity. We don't think natural resources will, will play a huge role in the short to medium term. So in short, growth miracles can happen. If you look at Czechia and Poland, where 30 years ago and now, uh, it's remarkable. They're, they're comparable in GDP per capita to some Western European countries. Productivity gains, but also capital accumulation, played a strong role. And Ukraine will need massive private capital inflows, structural funds, more domestic saving to create a virtuous circle.

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But this is a very safe bet for Ukraine. We have seen earlier examples. Will it work for Ukraine? Ukraine has done a lot. There's more to be done. But as Alina mentioned, um, civil society in Ukraine has evolved, and there's an overwhelming consensus regarding the EU, regarding, uh, banishing corruption, regarding becoming a westward-facing country. On the European side, Europe views Ukraine as part of Europe, not just a Russian buffer or a frontier with Russia. And of course, the extent that the EU can strengthen itself, raise its own game, enhance its own unity, the European project, including Ukraine, will be on a stronger footing. Coming back to the title, We feel that Ukraine now has a new chance to grow, to become a Western country, but this may be the last chance. And so we quote this haiku from Ian Fleming's James Bond novel, *You Only Live Twice*. You only live twice, once when you are born and once when you look death in the face. And with that, I will turn it over to Jacob.

[00:43:07.09] - Jacob Funk Kirkegaard

Well, thank you very much. I have to say, I wasn't expecting us to end on a James Bond link, but thank you very much, Maury, and thank you very much also to Alina and Yuriy for a tour de force of Russia and Ukraine in both short and long-term issues. I have one question already in the Q&A, which I promise I will get to. Very shortly. I would also encourage other participants to pose questions to the panelists if they have one. But I guess I will misuse my chair prerogative and ask the first one, which is one of the issues that neither really mentioned much, despite the fact that this is an issue that is almost ubiquitous in almost any other international economic development discussion at the moment, namely the role of China. So I guess the question I have to all the panelists, when you look at the role of China, both from a Russian but also Ukrainian perspective, obviously Russia has, I think most people would agree, gotten into an ever more intense sort of dependency on China, both as a customer of last resort and as a provider of technology and other types of support.

[00:44:38.01]

And even for Ukraine, at least initially, China has been a major supplier of parts and components to the Ukrainian scale-up of drone production. So I was hoping that either one of the panelists might be able to elucidate how they see China in any post-war development path for both countries play a role or not.

[00:45:14.28] - Elina Ribakova

Thank you.

[00:45:20.17] - Maurice Obstfeld

I'm willing to jump in with some conjectures if no one else wants to go first. Um, you know, China has historically not been hostile to Ukraine, and, um, you know, to some degree, the, the, um, uh, the current configuration in which, uh, there's a tight grip between, um, uh, Russia and China you know, the no-holds-barred partnership comes from their perceived need to have solidarity vis-à-vis the US. But, you know, we actually see the US disengaging from Ukraine, disengaging from Europe. The recent National Security Strategy statement from the US is more hostile to Europe than to Russia or China, which is remarkable. And so, to the extent that Ukraine does become a more integrated part of Europe and Europe raises its own cohesion and its independence of the US, I would see China in the future being eager to invest in Ukraine and do business in Ukraine. Not unlike the US, much Chinese policy is driven by commercial interests. And as I see the current situation as possibly quite temporary.

[00:47:04.20] - Yuriy Gorodnichenko

Elina?

[00:47:05.21] - Elina Ribakova

Maybe I'll jump in quickly that China has been indeed very opportunistic. If we look at the type of goods that China imports from Russia and exports to Russia, it imports mostly commodities. Which for Russia actually it is somewhat embarrassing because in 2000s Russia used to export to China more higher value-added products, maybe even sometimes machinery. But now it is almost entirely commodities. It's 83% is energy, then it's another 30% raw materials, and then there are some other things. In terms of what Russia imports from China, more than 40% is machinery. And that machinery, it doesn't mean that China is substituting away Western components. It is actually onshipping Western components oftentimes. And if you look at the

export controls evasion, over about 90% of export controls evasion happens one way or the other via China, including Hong Kong. It may be actual shipment, it might be production in China, joint companies or licensing, and then being onshipped to Russia. Or maybe it's company secretaries producing a lot of different companies in Hong Kong and then using those companies to onship to Russia. So China plays a very opportunistic role. Until recently, what we understood is China has been cautious not to cross the red lines on the secondary sanctions, but it is disturbing that of late we have heard China actually take a stake in a Russian drone producer and is being a bit more explicit in a way, basically very public and explicit in a way that it participates in the military-industrial complex.

[00:48:42.09]

So I think there is a risk that with US subsidizing on their on the secondary sanctions front threat that China maybe will get a little bit more adventurous. That said, China has not been investing in Russian economy at all. And I think that's my last comment is with everybody saying, well, if there is this peace agreement that there are Western company at the low start waiting to invest into Russia. Well, China has had ample opportunity to take advantage of investment opportunities in Russia, and yet it decided not to. And the most often quoted reason among Chinese companies is lack of a predictable business climate. I'll leave it here.

[00:49:22.13] - Yuriy Gorodnichenko

Okay, excellent.

[00:49:23.01] - Jacob Funk Kirkegaard

Yuriy, do you want to comment on— I know you had some connection problems earlier— about the potential role or not of China in Russia's longer-term economic future?

[00:49:39.27] - Yuriy Gorodnichenko

You know, I will say very quickly that, uh, based on our research with Smore, we know that economic growth is fueled by investment and technological transfer. It seems unlikely that China is going to offer the same generosity that we saw in Europe coming from Germany, France, Italy towards Poland, Czechia, and other countries. So even if China continues to be involved with Russia, it will be a very different relationship. It will be a very different growth model So I am pessimistic that China somehow can trigger massive increases in the growth rate of GDP in Russia or kind of gross of incomes more generally.

[00:50:23.28] - Jacob Funk Kirkegaard

Thank you. I'm going to go to some of the questions that we have in the Q&A. The first question concerns what is termed the sort of aid for equity swap, which is basically the argument that that if you entice Western participation directly on the ground in Ukraine, that will— the West's long-term commitment to the country. This is obviously some of the thinking that we will recall going back to the critical minerals deal with the Trump administration some months ago. Do you think that type of, you know, skin in the game, if you like, is a relevant factor when you think about both the commitment or lack thereof of the Trump administration and the EU to Ukraine in the long run? I don't know which of the panelists would like to start.

[00:51:31.14] - Yuriy Gorodnichenko

I, I can start by saying that we know this has not worked in the past. American companies made huge investments in eastern Ukraine and southern Ukraine. For example, Cargill had hundreds of millions of dollars invested in eastern Ukraine agribusiness. They lost a lot of money. That had zero influence on the stance of the U.S. government. The same applies to German firms and other firms who invested in eastern and southern Ukraine, again, they lost a lot of money. That did not affect the positions of their governments in any way. So I think it would be very naive to believe that somehow having an economic stake in some Ukrainian businesses is going to be a big factor in how Europe, US, or other countries are going to think about policy towards Ukraine, Russia, and so on.

[00:52:29.02] - Maurice Obstfeld

Yeah, I could, I could add, you know, if we think about the US, we sort of have to ask about the current regime and possibly future regimes. I don't see the Trump administration as being willing to, you know, intervene in the European theater in any way, particularly because it will also be trying to make investments in Russia. And, um, it's not clear it would tilt to Ukraine. Um, nor do I think future administrations, a Democratic administration, would go in to protect industries. I think the situation with respect to Latin America might be different. Uh, again, coming back to this national security memo, um, you know, there's a clear desire to protect and promote US interests in that region. And I think, you know, what happens in Europe is going to be pretty irrelevant to the Trump administration.

[00:53:31.27] - Jacob Funk Kirkegaard

Alina, anything?

[00:53:34.08] - Maurice Obstfeld

Okay.

[00:53:34.29] - Jacob Funk Kirkegaard

All right. We have another question that perhaps is most directly addressed to Maury or Yuri. It concerns the sources of financing in any economic recovery in Ukraine. I mean, you already alluded to it, I think, in your presentation, Maury. But the question pertains really to the sources of these, the funding needs. Does it come mostly from the private sector, international governments, multinational development banks, or other types of sources? What is your sort of, again, this will obviously be approximate beliefs.

[00:54:17.18] - Maurice Obstfeld

Yeah, I mean, I can start on that. I think that in the short run, we're going to see mostly official and multilateral institutional aid. The private sector has just restructured considerable debt. And while I don't think that is a long-term bar to investment in Ukraine. On the contrary, you know, we argue in the paper, Yuriy and I, that this has been useful in reducing debt overhang. I do think the private sector is going to want to see, you know, the fruits of official investment and the fruits of any peace agreement before coming in on a large scale. You know, given success and given some degree of stability over a couple of years, I think there is the prospect of much more extensive private investment in the Ukrainian economy.

[00:55:22.22] - Jacob Funk Kirkegaard

Anybody else?

[00:55:27.07] - Yuriy Gorodnichenko

One point I would add to what Maury said is that one was that the amount of money is totally manageable. Manageable, right? If we are talking about \$40 billion, it doesn't mean the World Bank has to come up with \$40 billion, or, you know, another institution has to come up with \$40 billion. You know, you can spread this across different institutions. Some of this may be World Bank, some of this may be European Investment Bank, it may be Council of Europe Development Bank. You know, when you allocate these resources across many, many potential financial sponsors, so to say. It's not a lot of money, it's doable. And then over time, as Maury said, we hope that, you know, a bigger role is going to be played by foreign direct investment. And so this financial institutions like World Bank and others, they don't have to be involved as heavily as we would like them to have in the early stages in the post-war Ukraine.

[00:56:23.27] - Maurice Obstfeld

In particular, accession to the EU would be a massive spur to private investment. And, you know, there's some discussion of that possibly being accelerated in any peace agreement. We don't know, but that would be a major factor.

[00:56:41.29] - Elina Ribakova

Maybe I'll just add very quickly that private sector debt is not going to make it or break it for Ukraine's debt sustainability. But I think it is critical what Maury and Yuriy have pointed out also in their paper, that it's important to remove the debt overhang and there has to be comparable treatment also with the any other restructuring. So having now money spent on repaying private sector debt, and especially if we want to discuss the warrants, and we will have experience of Argentina case here as well, that is completely, in my view as an economist, unacceptable because it neither sets up Ukraine for the better future to have the payout, it actually would remove the debt overhang and improve Ukraine's ability to attract investment in the future. And I think also that instrument itself, particularly in circumstances. So war is completely dubious.

[00:57:36.04] - Jacob Funk Kirkegaard

Thank you very much. But we have no more questions from the audience, and we only have a couple of minutes left. So let me ask you a relatively, a deceptively simple question, and you can just answer it, you know, with an almost yes or no. And it basically pertains to the sort of relative sources of economic uncertainty, because currently The European Union will, as we've talked about earlier, be— they're debating the so-called reparation loan. And the reparation loan is basically a commitment to fully fund Ukraine, cover any budget gap, including military procurement for 2 years. So basically, the rich uncle steps in to finance the war as needed, more or less. So will that, in your opinion, given everything that's going on in the Russian economy, shift the relative balance of economic uncertainty to the detriment of Russia, or will it remain with Ukraine? You only have time to give a very short answer to that question. Thank you. Who will start?

[00:58:52.04] - Maurice Obstfeld

I'd like to go last on that, but—

[00:58:53.18] - Yuriy Gorodnichenko

Okay, I can go first. Defense, and it will help a lot tremendously and will send a strong signal to Russia that they can't win this war. They have to stop. Thank you.

[00:59:07.25] - Elina Ribakova

I absolutely agree. I would just add, it would be— it's a unique moment for Europe to invest into defense in a smart way that will also have productivity spillovers on the civilian economy. So I think that also spending money this way allows Europe to boost its productivity alongside, let's drag in many other reports, but at the same time create credible deterrence vis-à-vis Russia or anybody else?

[00:59:34.23] - Maurice Obstfeld

Yeah, my complementary point would only be that this is, in my view, a make-or-break moment for Europe. If they can't make this happen, you know, getting these resources for Ukraine, the prospects of moving forward in terms of initiatives for greater European unity are going to look very dim, and Vladimir Putin will understand that message.

[01:00:02.04] - Jacob Funk Kirkegaard

Well, thank you very much. We are unfortunately at our witching hour, and I would like to thank the panel, Maury Oksfeld, Alina Rybakova, and Yuriy Gorodnichenko, for a very stimulating, interesting panel, and we We look forward to continuing to cover this very timely and pressing issue really for not just Europe, but certainly the global economy in the month. So without further ado, thank you to the panel. Thank you for all, to all of you that are, that join the panel online and meeting adjourned.

[01:00:45.11] - Maurice Obstfeld

Thank you.

[01:00:45.25] - Elina Ribakova

Thank you.

[01:00:47.04] - Maurice Obstfeld

Thank you.