

Understanding the Effects of the Russia-Ukraine Conflict on the Global Economy

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Abstract

The present paper outlines how the Ukraine-Russia conflict has proven to be something beyond the humanitarian crisis. Since the war has started, the risks to financial stability are increasing, and the after-effects of Western countries' huge sanctions against Russia can finally be observed and analyzed. The article sets the record straight by explaining in detail how the war between the two countries has caused the current economic crisis.

Key words: global economy, ukraine-russia conflict, economic crisis, labour market, inflation rate

J.E.L. classification: F01, R53, E24

1. Introduction

From a general perspective, war always brings several issues, challenges, and unseen repercussions due to the demolition that it causes. The nature of these "issues" could be classified as social, humanitarian, psychological, economic, etc. How deeply it affects all aspects of life depends on the amount of destruction that results due to the events that take place and many different factors, such as the intensity of the situation, countries' resilience etc. However, the present paper discusses and focuses only on the economic aspects of the war between Russia and Ukraine, which started on 24th February 2022 (DW News, 2022).

2. Theoretical background

The Russian invasion of Ukraine raises strong questions about global security and the economic system. Due to globalization, the consequences of this war cannot be expected to remain limited only to one part of the world. Whatever is happening in Ukraine is also experienced by all countries' labor markets, supply chains, economic growth, stock markets, etc. (The World Economic Forum, 2022). Therefore, one may conclude that the economic impact of this humanitarian crisis is felt globally. It is so interesting to note how volatile the market is. Any unprecedented event has the potential to shake the global economy. For the same reason, it is critical (especially for investors and financial decision makers) to understand what is going on in the market in order to make better and more informed decisions in order to avoid financial difficulties.

One must also pay attention to the time frame in which the war started. It is relevant because it followed the COVID-19 pandemic. The economic recovery from the pandemic was the first concern of the concerned authorities till the news of war suddenly broke. The Russian invasion of Ukraine further complicated the COVID-19 economic recovery even more (The United Nations, 2022). Following the invasion, many Western countries issued unprecedented bans and huge sanctions on Russia (Bloomberg, 2022). How this "move" will affect Russia is also a colossal topic of discussion.

In this context, the present paper contributes to a better understanding of the impact of the Russia-Ukraine war on the economy as a whole. The main goal of this paper is to provide a concise report on the topic by analyzing what various scientific papers and news articles share about this subject.

3. Research methodology

A literature review methodology has been used to evaluate the present subject. Since the conflict is still ongoing, the information or data included in this engaging paper is as up-to-date as possible and sourced only from credible sources (such as the UN, BBC, ILO, CNBC, and so on) to ensure the topic's relevance for the readers.

As this is a sensitive topic for many people, the research has been done in an objective way with a focus on the economic aspects of the current issue. The geopolitical aspects have been completely ignored because they are not the focus of this research.

4. Findings

From a soaring food crisis to sky-rocketing inflation rates, the fallout of the Russia-Ukraine conflict has had its impact on almost all the economic aspects. In the following section, we will study how the war affected prices, the stock market, inflation rates, the labor market, and economic growth.

As Carmen Reinhart, Chief Economist of the World Bank, states on inflation, the pressure that the Ukraine-Russia crisis brings to bear at a time in which inflation is already concerning means that the uphill battle is even more uphill (Financial Times, 2022). This statement best describes the current situation. For quite some time, even before the war between Ukraine and Russia began, the topic of inflation was in the headlines of many well-known news forums and business magazines. Analyzing different articles, one may draw the conclusion that on today's date the inflation rates of many different countries, including France, Slovakia, and Germany, have hit a new record (Reuters, 2022; IntelliNews, 2022; Business Standard, 2022).

A crucial factor in the inflation rate may be the lack of energy supplies from Russia and food shortages from Ukraine. This can cause a supply shock, which in turn will lead to additional inflation (VoxEU, 2022). Therefore, inflation is an ongoing issue for many investors and policy-makers. Investors are flustered by rampant inflation and its consequences. The International Monetary Fund predicts the U.S. inflation rate will reach 7.7% this year and 5.3% in the euro zone. (CNBC, 2022). The worst is yet to come, as the National Institute of Economic and Social Research (NIESR) made a prediction regarding the aggravating economic circumstances, stating that real disposable income might drop by 2.4% this year (Forbes, 2022). But, along with the economic effects of the war in Ukraine, it is also thought that the recent "inflation surge" was caused by rapidly rising energy and fuel prices (Forbes, 2022).

Figure no. 1. Russia: Inflation rate in Russia compared to previous year



Source: (Statista Research Department, 2022)

Figure no. 1 is a graphical representation of monthly inflation rates in Russia compared to the same month of the previous year. It is evident from the given graph that Russia has gone through a gradual increase in inflation rate in this one-year span (starting from April 2021 till April 2022) till February 2022 (Statista Research Department, 2022). In March 2022, Russia went through the highest inflation rate increase over the course of this period. This "sudden growth" may be justified by the fact that the war between Ukraine and Russia started in February 2022.

As a matter of fact, since the news broke-out, many chose to flee the country, and according to a recent update, more than 14 million people are thought to have already fled their homes since Russia's invasion of Ukraine in various countries like Poland, Romania, and Hungary (The BBC News, 2022). This key piece of information is crucial because, due to this migration, 5 million jobs have been lost (The International Labour Organization, 2022). This crisis has been putting pressure on labour markets and is increasing unemployment rates, as the UN states in one of its reports (The World Economic Forum, 2022).

Although the direct consequences of COVID-19 are considered to be health-related, their impact on the economy is enormous (Palomino *et al*, 2021, p.2). Several scientific papers support the idea that the labor market has gone through a shock due to the COVID-19 pandemic. In the US, the unemployment rate stood at 14.7% in April 2020 (Borjas *et al*, 2020, p.2).

Unemployment is a humongous issue that even Russia is facing today. Many employees are becoming jobless since companies are fleeing Russia. As per a report of the Centre for Strategic Research, in February 2022, 3 million employees were estimated to be unemployed, while 2 million jobs are still at high-risk this year (Quartz publication, 2022). Therefore, the war has had a strong negative impact on the labor market, which is being felt by the citizens of both the countries involved. Obviously, with fewer job opportunities and more people getting unemployed in Russia, its impact will also be felt on the Russian economy.

Regarding the stock market, it is impossible in today's world to imagine a world without stock markets. In a market economy, the capital market plays the most important role. The stock exchange market acts like a barometer because it reflects the present situation of the economic field. However, one must also keep in mind that even the stock market is sometimes capable of generating false signals that are contradictory to the real-life situation (Andrieş, 2009, p.71). Researchers share different views regarding this topic (Masoud, 2013, p.2). Although it is the simplest and shortest way to analyze what is happening to the global economy.

According to a scientific article, the stock markets had already seen a negative impact from a number of lockdowns because of the international travel restrictions (Hatmanu *et al*, 2021, p.3). The stocks were falling throughout the year due to the fear of inflation and the likelihood of higher interest rates during the pandemic period (BBC News World, 2022).

The world economy was already going through a hard time. But, the Russian-Ukrainian war has brought more uncertainty to the stock market, which already had an unsteady beginning this year (Time, 2022). So, there is no getting around the fact that the Russian invasion of Ukraine has rattled global markets (Investopedia, 2022). Talking about the present-day situation, the stock market today is more volatile than ever before because of several factors, such as the sudden price increase of oil and gas, rapidly increasing inflation rates, etc.

Just as the global economy began its journey towards recovery from the COVID-19 pandemic, the Russian invasion brought in another new challenge. Although at first glance, Russia and Ukraine seem to have a comparatively smaller part of the world economy, they both account for a bigger part of global energy exports, which is also the reason why many European countries' reliance on Russia's oil and gas is a substantial issue (The Business Review, 2022).

According to a report by the International Monetary Fund (IMF), the world economy will grow at a slower pace because of Russia's invasion of Ukraine. It is estimated that economic growth, which was 6.1% last year, will fall to 3.6% this year (The VOA News, 2022).

There are several claims that the Russian and Ukrainian economies will shrink by a large percentage in comparison to last year. The IMF predicts the shrinkage of the Ukrainian economy by 35%, while the World Bank expects a 45% contraction (The VOA News, 2022; The World Bank, 2022). On the other hand, Russia's economy is believed to be already in "deep recession" due to the heavy sanctions by the West (The World Bank, 2022). The previously mentioned estimates confirm the war's long-term negative effects on global economic growth.

5. Conclusions

To summarize, the economy is going through a rough time as it has experienced many downfalls in the past few years due to various unprecedented events. Even before the war broke out, investors and policy-makers were facing numerous challenges (like lockdowns, the arrival of new COVID-19 strains, soaring inflation, monetary policy, and central bank frameworks) to aim for recovery (VoxEU, 2022). However, the Russian invasion aggravated the circumstances, making it more challenging for the economic recovery to take place.

Following the outbreak of the war, inflation rates rose rapidly (for example, in Russia, see figure 1). People suffered as unemployment rose, the economy suffered, and supply chain issues were exacerbated, resulting in higher inflation rates. It is important to note that recovery is a slow process and proper measures need to be taken to quicken the pace of economic growth.

As a matter of fact, the present crisis has been successful in creating tension among the countries, and it appears to be a provocation and a cause of concern for many European countries that are dependent on resources from Russia and Ukraine. The countries will feel the void due to the shortages of food, oil, and gas supplies till they find a better alternative.

The situation is also a lesson to be learned for the upcoming generations (and especially for policy-makers) to keep in mind the importance of global security and maintain good relations with neighboring countries. Because, practically speaking, in today's global era, it is unwise to think of surviving without a good geopolitical strategy. It is a modern weapon that countries need to start using, not only to maintain peace and harmony but also for the sake of long-term global growth prospects.

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