



UKRAINE QUARTERLY REPORT

Q2 2025

Expect greater European support along with some US support, as the economy revives mildly

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Executive Summary

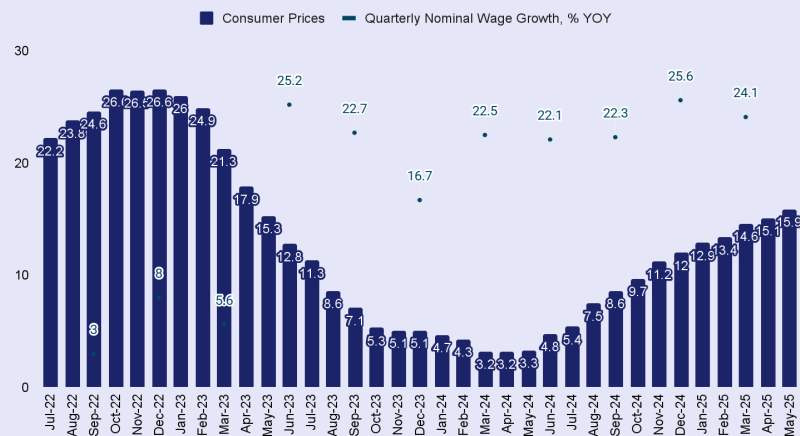
Expect greater European support along with some US support, as the economy revives mildly

As anticipated, ceasefire talks have effectively died; however, a land-for-peace deal over the longer term remains the most likely scenario, given our confidence in Europe stepping up to provide for both Ukraine's and its own security and defense. As before, investors should monitor further demonstrative steps of European nations supporting Ukraine, including defense aid as well as extending sanctions in July, ensuring Russia's FX reserves do not revert back to Russian control. We retain cautious optimism regarding upcoming tighter US sanctions on Russia's oil exports (aligned with EU sanctions) as well as more US military support coming via purchases from Europe. Regarding the economy, growth is gradually reviving after a slow winter of power outages and high inflation. As business costs and consumer prices stay higher-for-longer, and the labor market remains a challenge, demand will improve but remain restrained.

BUSINESS TRENDS

CONSUMERS

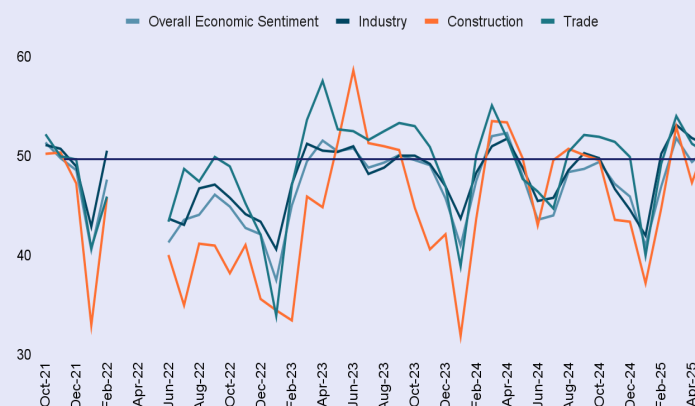
Strong income growth will outpace inflation and drive spending again in 2025



BUSINESSES

Investor sentiment has revived after a challenging winter

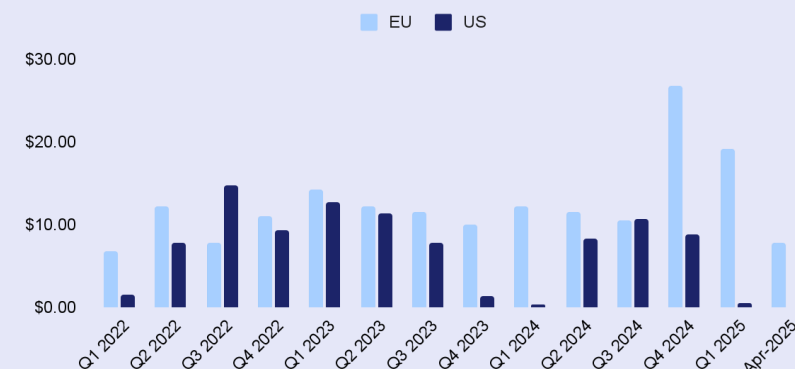
Business Activity Expectations Index (above 50 indicates optimism)



GOVERNMENT

European aid has picked up notably and will be adequate for the 2025 budget

Western aid, € bn



Forecast Summary

Forecasts as of June 25, 2025, subject to monthly revision

	2023	2024	2025f	2026f
GDP, %YOY	5.5	2.9	2.8	5.1
Inflation, %YOY	12.9	6.3	12.2	7.4
Consumer Spending, %YOY	4.3	6.8	4.9	6.1
Investment, %YOY	48.1	8.9	12.0	17.5
USD:UAH (avg)	36.80	40.11	42.00	45.10

Economic Outlook for Ukraine

Growth looks steady for this year, with rising uncertainty and higher-for-longer inflation restraining sentiment

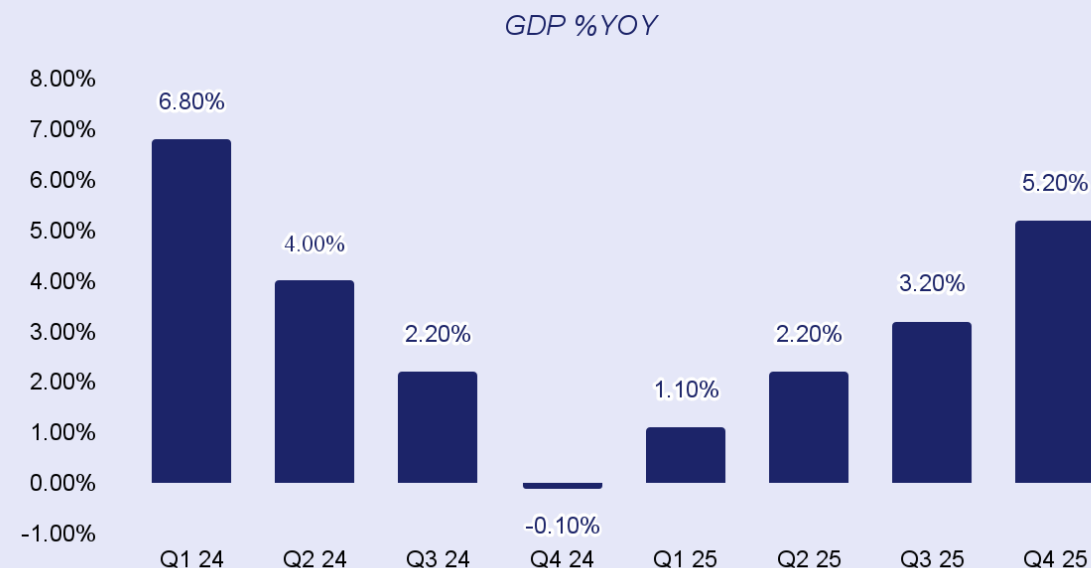
LATEST ECONOMIC TRENDS

- While business sentiment has picked up consistently since February, GDP growth remains moderate: in Q1, growth was just 1.1% YOY, with government and consensus forecasts at 2.5-3.0% YOY for 2025. Consumer spending has remained the primary driver of growth, even amid accelerating inflation across H1; however, business activity has struggled with industrial production down 6% YOY and exports down 7% YOY in Q1 (and neither improving in Q2). High consumer prices (15.9% YOY in May, the highest level in two years) and producer prices (over 40% YOY in March and April) weigh on sentiment, but have likely reached their peak with expected price moderation in H2.

2025/2026 OUTLOOK FOR UKRAINE

- Businesses should still expect a land-for-peace deal over the long term. While there is no realistic expectation for a ceasefire in the near term, we continue to believe Russia will be compelled to pursue a ceasefire by early 2026, assuming tougher Western sanctions imminently, as we do. Likewise, investors can take comfort in Europe's rapid reaction to support Ukraine amid US disengagement.
- External financial support looks solid for Ukraine through 2025 and deep into 2026, thanks to European support to fill the expected gap in US funding. Even in the event of a lack of US military support, a combination of Ukrainian domestic production and the ongoing rapid increase in European support will be adequate to protect Ukraine and resist Russian air and land aggression.
- The economy picked up moderately in Q2 and will continue to revive across H2, albeit restrained by high prices and uncertainty. Inflation has likely hit its peak and is likely to moderate starting in Q3. The hryvnia will remain more stable than initial forecasts, allowing for greater consistency in import prices. Consumer demand will remain the backbone of growth thanks to solid income growth.
- The major risk to the outlook relates to Kyiv's reduced ability to deter long-range strikes from possible loss of US air defense. Meanwhile, the very tight labor market will continue to drive up business costs and worsen staff shortages.

The economy has gone through its worst moments, and should revive in H2



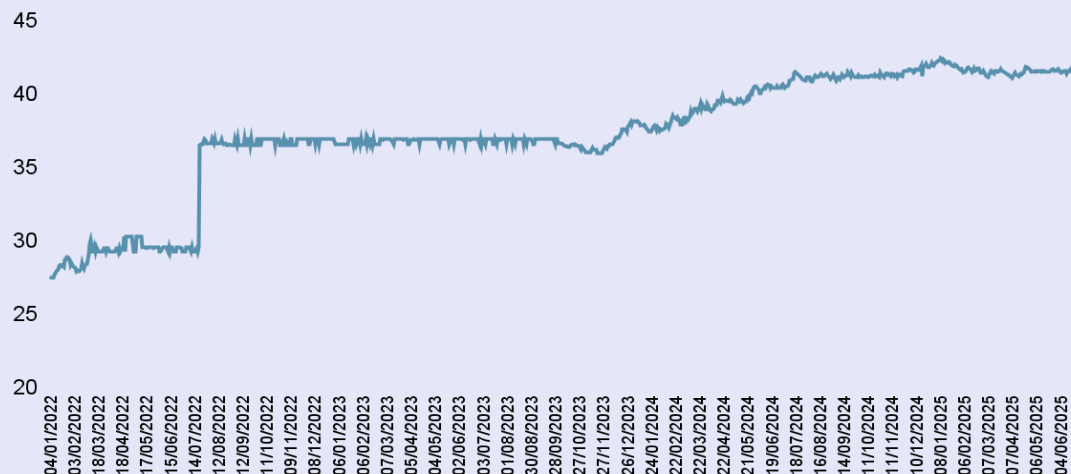
Hryvnia Tracker

The hryvnia should remain stable in H2 now against the dollar, but more weakness is coming against the euro

- The hryvnia has been stable and steady for the past year thanks to strong and consistent outlays of Western support. Though questions remain related to US support, European and aid from other nations remains set to fill that gap. As a result, the central bank felt confident to support the currency strongly in H1. The central bank remains determined to support the hryvnia amid elevated inflation this year, and despite a worsening current account balance in H1 from rising imports and falling exports. Depreciation has now been pushed off to 2026, though will be mild. Businesses should factor a weaker hryvnia next year in their business plans and contracts with suppliers.
- Critical to hryvnia stability is continued Western financial support, which pushed reserves to record levels, amounting to ~\$45 bn in May. Reserves will rise beyond \$50 bn by the end of the year, cementing macroeconomic stability.
- Positively, the major risk to the hryvnia's outlook – cuts in US aid – is not a significant concern for the next year given Europe's determination to provide funding to Ukraine at either the bilateral or EU-wide level. Should we see a cut in US funding, Europe will fill the necessary financing gap.
- More concerning, the hryvnia will continue to weaken notably in the months ahead against a surging euro, which is benefiting from a weaker dollar amid Trump's tariffs.

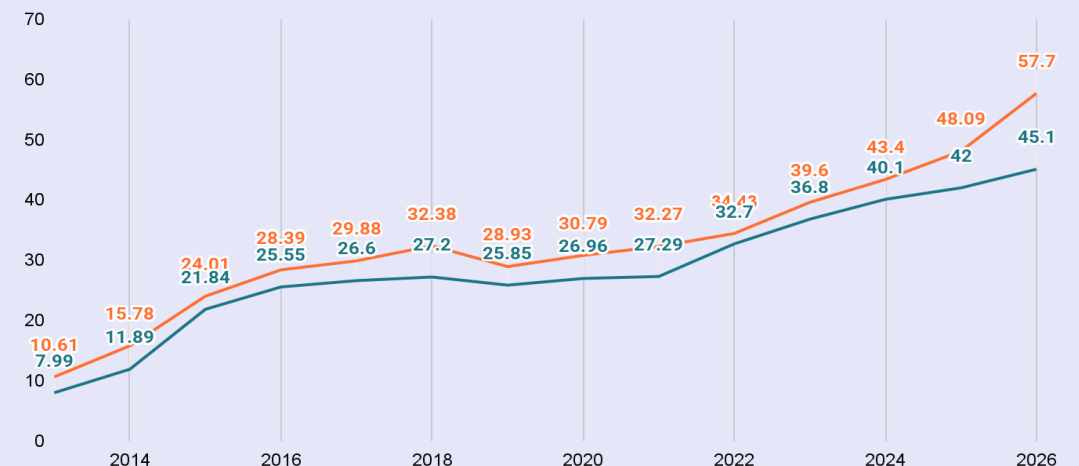
The central bank will continue to support the hryvnia the rest of 2025, pushing depreciation into 2026

USD:UAH



The hryvnia will weaken further next year, though with limited impact on inflation

EUR:UAH USD:UAH



Operational Environment

Prepare for a wide range of scenarios amid a prolonged war and uncertainty

OPERATIONAL ENVIRONMENT OUTLOOK

As expected, the ceasefire talks since the start of the year have failed, leaving continued uncertainty and a prolongation of the war through 2025 as the base case scenario. As a result, the operational environment will remain challenging the rest of 2025 and into 2026.. Labor market pressures will only further intensify while the energy network has been damaged and continues to be attacked. Matched with uncertainty related to a Trump presidency and sustained intense attacks along the front, investor sentiment at headquarters is weak, delaying investment. More positively, cost pressures should start moderating, providing some relief to businesses.

NO CHANCE OF CEASEFIRE NOW, THOUGH RISING PROSPECTS INTO 2026

- Putin's disinterest in a ceasefire has become clear, though to date the Trump administration refuses to place any notable pressure to compel him to stop the fighting. As long as Putin believes he is winning and faces no major pressure from the West, a ceasefire is unrealistic. Under our belief, however, of stronger US and EU sanctions and further military support to Ukraine, Putin will be under more pressure to consider a ceasefire by early 2026. *For more on this, see the MAJOR TOPICS section below.*
- Investor optimism related to the end of the war has moderated as well. Polling at our UBN Network event in June noted that 63% of attendees believe the war will only end in 2027 or later. Only 43% believe Trump will continue to provide support, which would be necessary to stop Russia and achieve a ceasefire, and 57% believe he will abandon Ukraine – a marked rise in skepticism regarding US policy.

TALENT MANAGEMENT

- HR issues continue to dominate internal decision-making, as has been the case across last year as well. Tens of thousands more soldiers are needed, indicating that this pressure on talent is set to only worsen the rest of the year and into 2026. The vast majority of firms struggle from staff shortages. The most in-demand roles largely consist of blue-collar specialties, e.g agricultural tractor driver, mechanic-repairman, welder, electrician, nurse, motor vehicle driver, and seamstress. Anecdotal evidence indicates that in recent months job seekers' salary expectations are becoming more unrealistic.

ROLLING POWER OUTAGES

- Severe damage to energy infrastructure from Russian shelling last winter has reduced Ukraine's capacity permanently. As a result, while the market has performed well lately amid lower energy demand, issues related to power generation and therefore manufacturing will build again this coming winter. Positively, businesses have procured their own power generation in large numbers, which will contribute to their resilience again this coming winter..

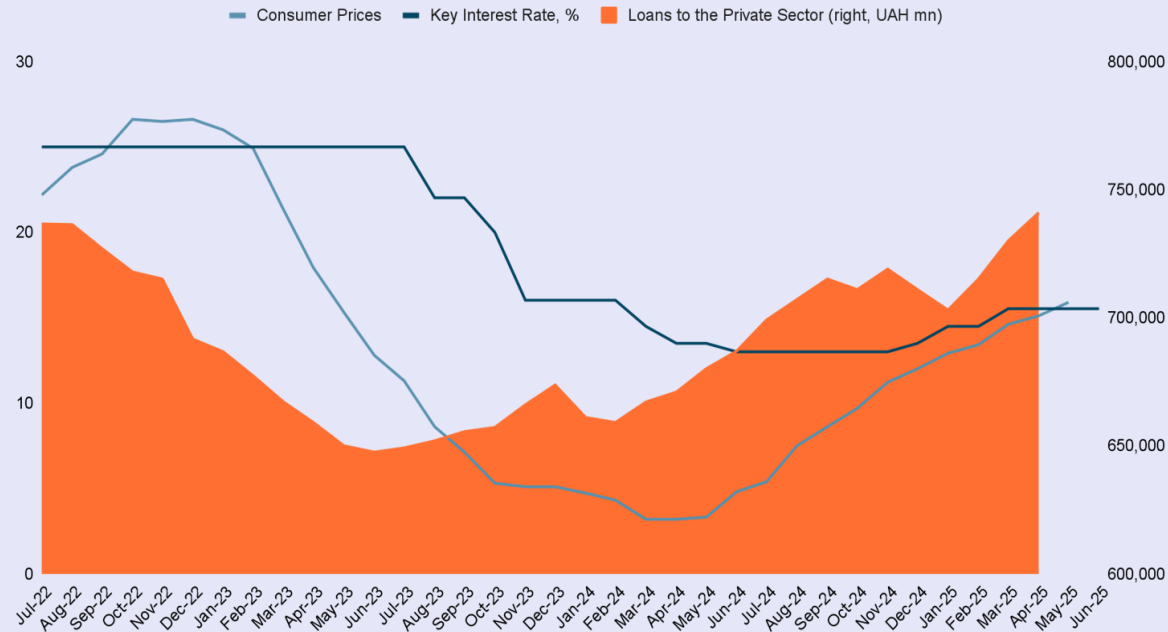
MODERATING COST PRESSURES

- Though inflation and producer prices have accelerated across H1, cost pressures for businesses should start to moderate in H2. As a result, interest rates on loans (key rate currently at 15.5%) will likewise fall, improving financial capacity for companies. Still, accumulated price growth of the past few years will weigh on business sentiment. Difficulties in raising prices on hesitant customers will continue to weigh on margins as well.

Operational Environment

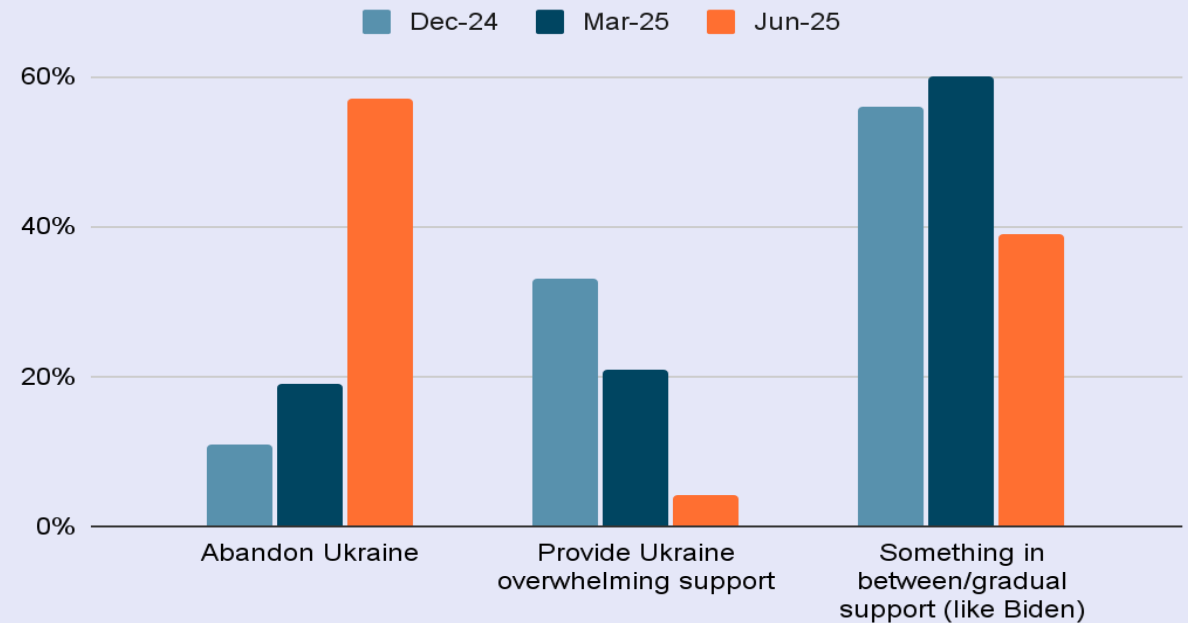
Prepare for a wide range of scenarios amid a prolonged war and uncertainty

Lending has picked up again in recent months, despite inflation outstripping the key interest rate



What will Trump do?

UBN Network Polling





DEMAND OUTLOOK

Consumer Demand Outlook

Solid income growth will continue to drive spending in 2025, despite inflation

OUTLOOK FOR CONSUMER DEMAND

- Consumer spending remains the primary driver of economic growth, thanks to high wages, and spending has persisted solidly even amid elevated prices this year. After retail sales rose by 12% YOY in 2024, sales slowed to 5% in Q1 2025, though largely due to high base effect. Consumer confidence began to revive solidly in February, then hitting its highest level in more than a year in March and April. Further income growth from the exceedingly tight labor market will continue to sustain the spending growth in H2 and into 2026.. B2C firms can plan for continued demand growth in H2, though likely without an acceleration.

KEY DRIVERS

Labor Market:

- Job-seeking has picked up considerably in H1 2025, compared to 2024 levels. Meanwhile, job vacancies have stabilized in the same period, indicating on the one hand a smaller labor shortage than last year while on the other hand no rise in opportunities. Unemployment has fallen from around 17% in 2024 to under 14% currently, and is expected to decline further the rest of the year, further tightening the labor market and sustaining wage growth. While positive to sustain consumer spending, consumer-oriented industries are facing some of the toughest challenges in the war for talent, impacting profitability amid rising labor costs.

Incomes:

- In Q1 2025, real wages (after inflation) rose by ~10% YOY, following ~16% YOY in 2024. Wage growth assuredly continued to grow solidly in Q2 2025, though likely to moderate in H2 due to the high base of 2024 and high (albeit slowing) inflation. Surveys and anecdotal evidence suggest the vast majority of Western firms are raising salaries above inflation, as they did in 2024 given the war for talent. High incomes support confidence: consumer confidence has picked up consistently in H1, reaching the highest levels seen since late 2023, and should pick up further in Q3.

Consumer Prices:

- Consumer prices have accelerated rapidly since late 2024 and across H1, hitting 15.9% YOY in May. The worst of the price growth appears over: after prices rose by nearly 2% in month-on-month (MOM) terms in late 2024, prices rose by only 1% MOM each month from January through May 2025. Inflation should start to moderate by H2 largely also thanks to the high base effect of 2024.
- Still, high food prices, at 22% YOY in May, remains the main driver of inflation due to a slightly weaker harvest and power outages which impacted food processing. Businesses are also increasingly forced to pass on their high producer prices, which have averaged ~40% YOY Jan-Apr., driving up consumer prices. Elevated labor costs and higher import prices on account of a strong euro have contributed to the price growth.

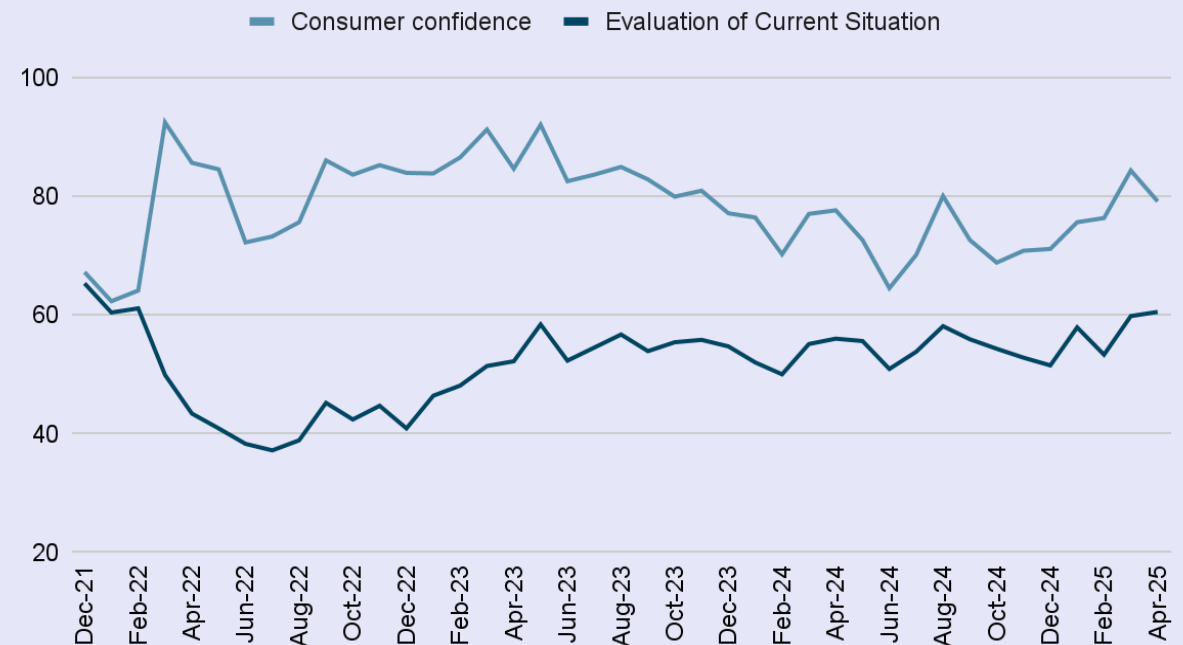
Consumer Demand Outlook

Solid income growth will continue to drive spending in 2025, despite rising inflation

Strong income growth will outpace inflation and drive spending again in 2025



Confidence has revived thanks to seasonal factors and despite inflation



Business Demand Outlook

Operations and demand will remain under pressure in the months ahead

OUTLOOK FOR BUSINESS DEMAND

- The primary issues impacting demand and operations relate to elevated costs (energy, labor, food) and talent management, both of which will continue to dominate business planning the rest of 2025. The prolonged nature of the war and ongoing uncertainty further weigh on sentiment. B2B firms will see demand continue, albeit without a notable uptick until there is greater clarity around a possible ceasefire perhaps by early 2026. Costs will weigh on margins given the rising difficulty in passing costs onto customers.

KEY DRIVERS

Recent Performance:

- Business sentiment improved again May, with all sectors reporting positive expectations in the months ahead. After a slight drop in April, the central bank's business expectations index rose to 50.8 (above neutral level of 50) from 49.4 in April, driven by strong consumer spending, stable energy supplies, and seasonal factors. Still, labor shortages, inflation, and continued air raids limited the optimism. The construction sector was the most positive thanks to a strong rise in volumes and new orders as well as purchases of materials. Industrial firms have seen 4 months of continued positive demand expectations, while retail has seen three months of optimism in a row, though still planning to cut margins to remain competitive.

Segmentation by Sectors:

- Through April, overall industrial production fell by 6% YOY, after rising by 4% YOY in 2024. A 16% YOY drop in mining output, given the loss of the nation's only coking coal producer, led the decline. Meanwhile, manufacturing was more resilient, falling by nearly 3%. Thus far in 2025, textiles/clothing, metals manufacturing, chemicals, pharma, and rubber/plastics have been the strongest performers. Meanwhile, food/drink – earlier the most resilient of sectors since the full-scale invasion – has seen a moderation, dropping by more than 10%.

(cont'd) Export-related sectors (e.g. agriculture, raw materials) will remain consistent thanks to improved trade conditions. In 2024, the agriculture sector achieved its pre-war volume of exports, totaling \$24.5 bn, despite output falling by 6% from 2023's record levels. Agriculture output is expected to stagnate at best this year, sustaining but not creating opportunities.

Cost Pressures:

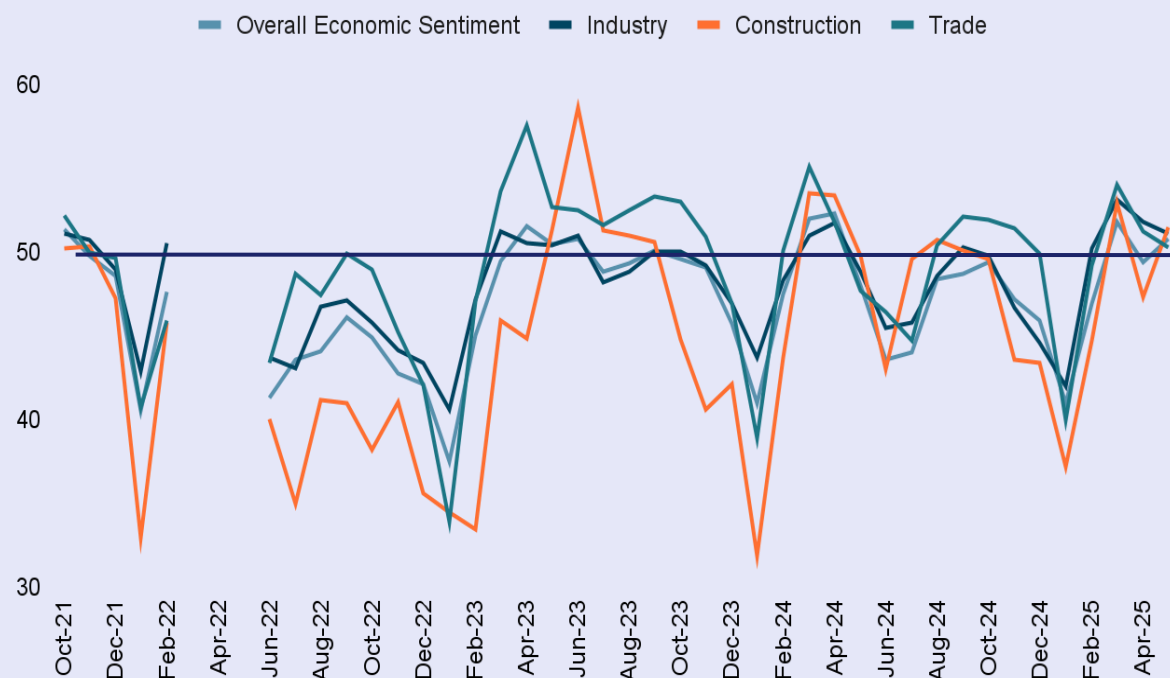
- Businesses are under notable cost and margin pressure, with producer prices still elevated. After a moderation across H2 2024, producer prices have picked up again and hit their highest level in two years, at 52% YOY in March and 42% YOY in April. High wages, food prices, and import prices from a strong euro are raising costs, which have to be passed onto customers. Positively, most sectors expect price growth to slow in the coming months.
- While credit costs remain elevated with the key rate currently at 15.5%, corporate and consumer lending has in fact picked up in H1 and should rise further in H2. With non-performing loans coming down and the profitability of the banking sector strong, banks are willing to continue to extend loans while borrowers now face a low real interest rate amid elevated inflation, driving credit growth.

Business Demand Outlook

Operations and demand will remain under pressure in the months ahead

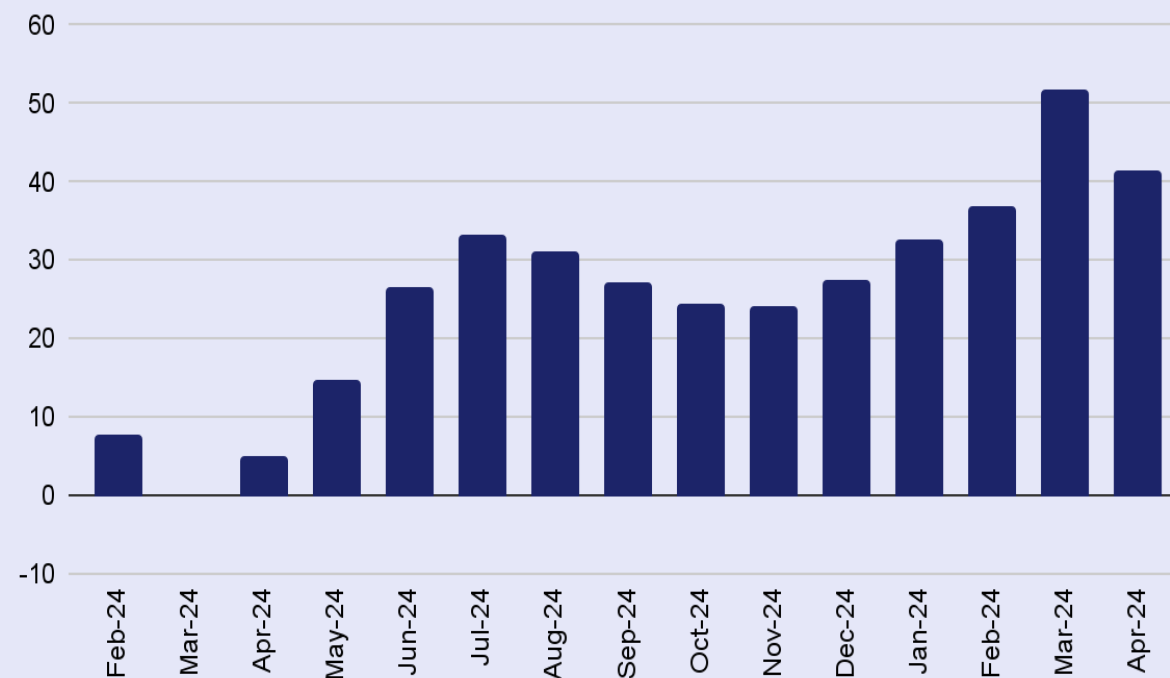
Investor sentiment has revived after a challenging winter

Business Activity Expectations Index (above 50 indicates optimism)



Already high costs for businesses further accelerated in H1

Producer Prices, %YOY



Government Demand Outlook

Budget funding remains solid for 2025, despite concerns over US support

OUTLOOK FOR GOVERNMENT REVENUE

- The US's suspension of aid in Q1 has naturally raised concerns about Ukraine's fiscal future. Positively, prior to this, the Biden administration fast-tracked much-delayed aid prior to Trump's inauguration, while in response to Trump cutting off aid European countries have stepped up with far greater financial and military support pledges. Critically, the German government removed its debt brake and has passed a major defense and infrastructure bill, with far greater funds promised to Ukraine.
- Strong promises of Western support had ensured Ukraine's fiscal outlook for 2025 and for most of 2026. In particular, promised rising allocations thanks to the G7's \$50 bn Extraordinary Revenue Acceleration (ERA) facility ensures Ukraine's macroeconomic stability this year. Foreign aid could rise to \$55 bn this year due to the expedited receipt of aid from the ERA and from the EU through the Ukraine Facility program. Ukraine's main European partners have recognized the need to support Ukraine as a matter of European security in light of the unreliability of the US.
- Domestic tax revenues are set to be an increasing share of total spending, expected to be 50% in 2025, up from 45% in 2024. A push to reduce the shadow economy will be vital, and has been somewhat evident as both personal and corporate tax receipts have risen this year relative to last year, and will be critical in filling budget gaps in 2026.
- Longer term, we remain optimistic the West will seize Russia's frozen fx reserves amounting to over \$300 bn. Europe's recognition of its need to provide for Ukraine on its own will compel the EU to seize the funds. In this case, Ukraine's budgetary and military needs would be financed for years.

OUTLOOK FOR GOVERNMENT SPENDING

- In 2025, budget spending will again be dominated by defense and national security spending, approaching some 60-65% of total spending as in 2024. Total spending is roughly stagnating in real terms, though as a percent of GDP is in fact falling from roughly 50% to 45%. With strong revenues thanks to the ERA facility and planned controlled expenditures, the deficit is set to fall in 2025 to 19% of GDP from 24% in 2024.
- For 2025, defense/security spending is rising by more than 2% YOY (UAH 2.22tr, from UAH 2.18tr). Non-defense areas (healthcare, education, social spending, etc.) are seeing consistent outlays in 2025 as in 2024 and will be funded by additional taxation and coming Western aid.
- Through April 2025, the largest expense was defense, as expected – amounting to roughly 60% of all expenditures and in line with budget plans. The government approved a draft amendment to the 2025 state budget, which allocates nearly ₪449 bn (\$10.8 bn) more in spending. Of that amount, a bit more than half (₪250 bn) will come from increased borrowing in the domestic bond market. The rest is expected to be sourced from external partners, likely front-loaded from aid intended for 2026.
- Even in the event of a ceasefire in early 2026, as we believe may be possible, there will be no major revisions to defense spending. Defense spending needs will be elevated for the long-term as a large standing army and high military spending will be required to protect against future Russian aggression.

Government Demand Outlook

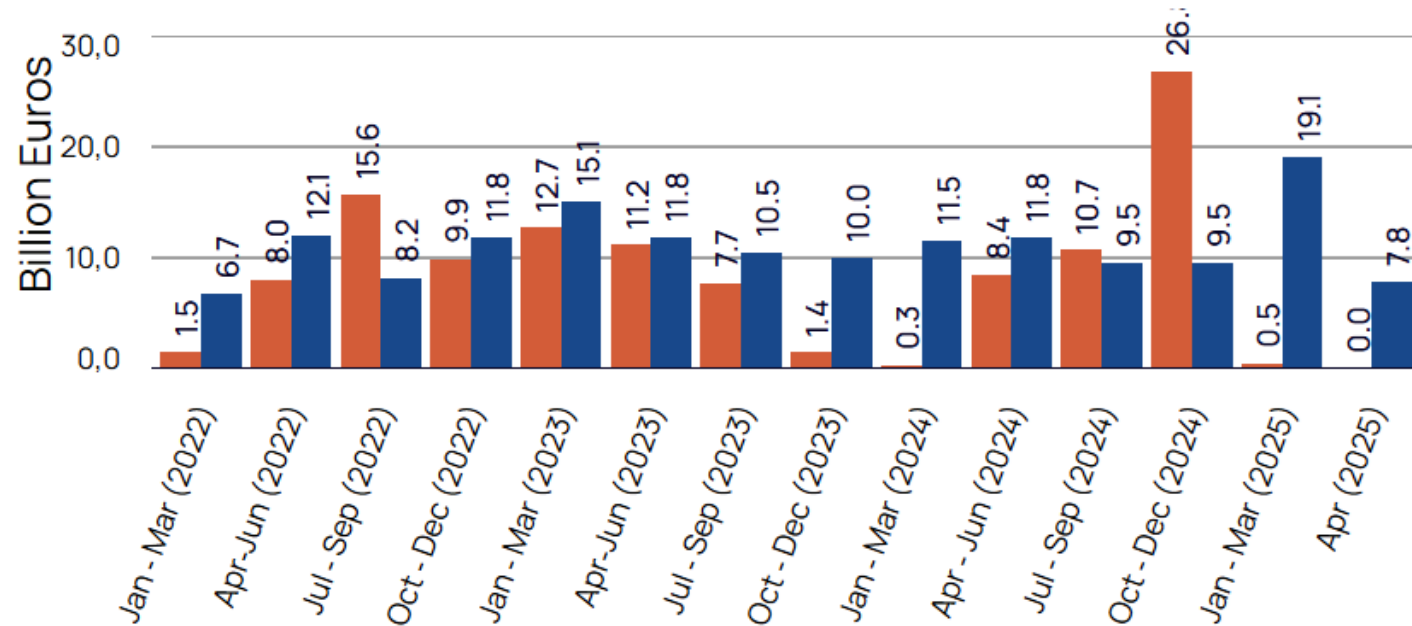
Budget funding remains solid for 2025, despite concerns over US support

European aid has picked up notably and will be adequate for the 2025 budget

Western funding, € bn Kiel Institute for the World Economy

Allocations January 24, 2022 to April 30, 2025

United States Europe





MAJOR TOPICS

Global Topics: Tariff Wars & Israel-Iran War

Tariff Wars and the Israel-Iran War have positive and negative impacts on Ukraine, respectively

Major shifts in international trade and the Middle East have repercussions for Ukraine.

However, the fundamental, critical impact for Ukraine relates to the trajectory of oil prices. Positively, Trump's tariff wars have an overall beneficial effect as lower global trade weighs on oil prices, hurting Russia's finances. On the other hand, the Israel-Iran War is a net negative for Ukraine as it raises oil prices. Ultimately, as we anticipate lower oil prices over the long term and US interest in limiting the scope and duration of the Israel-Iran War, Ukraine should benefit from these global forces.

- **Tariff Wars:** Trump for decades has viewed trade deficits as a core structural economic problem to correct, and therefore is determined to implement tariffs. As a result, while some backdowns related to China and others are apparent, higher US tariff rates against all trade partners will continue to weaken global growth, weighing on oil prices. Other negative effects (weaker Ukrainian and European growth levels, e.g.) are clear though are outweighed by the positive impact for Ukraine of lower oil prices, which dropped ~15% as a result of the tariff wars.
- **Israel-Iran War:** Israel's attacks on Iran limit Tehran's ability to support Russia; however, Iranian support to Moscow has been limited since helping Russia set up domestic drone manufacturing in 2022. Meanwhile, oil prices quickly rebounded at the outset of Israel's attacks on Iran's nuclear infrastructure, but within days moderated back under \$70 as markets believe the war will be contained given Iran's weak retaliation so far and Trump's interest in limiting the scope of the war. Worryingly, if the war drags on, oil prices would remain elevated and Putin may become useful diplomatically to Trump, reducing the likelihood of US sanctions on Russia.
- **Oil Prices:** Irrespective of these two phenomenon (and others assuredly to come), global oil supply and demand trends set out a clear downward trajectory for oil prices over the long term. Assuming tariff wars the next 3.5 years of Trump's term and a moderation of the Israel-Iran War over time, the net impact for Ukraine should be positive as oil prices should remain below Russia's budgeted oil prices. Expected tighter US/EU sanctions on Russia's oil exports will further weigh on Russia's oil export revenues.

Strong US opposition to another Middle East war should help limit an expansion of the conflict

Do you think the U.S. military should get involved in the conflict between Israel and Iran? (%)

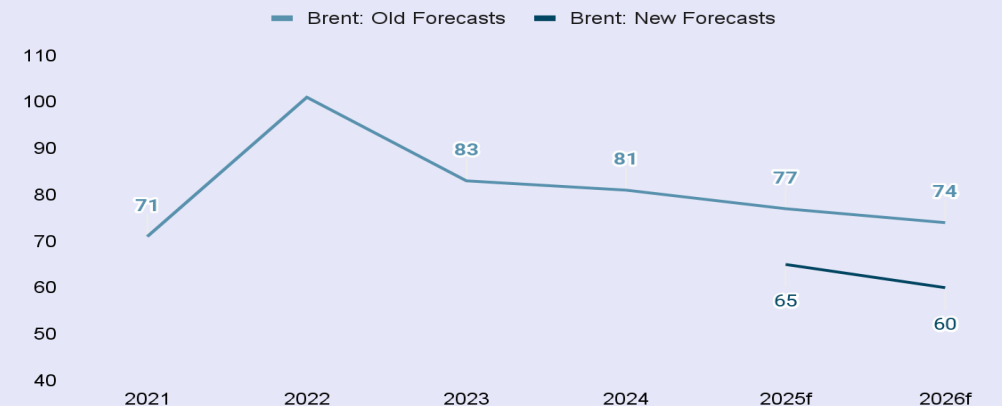
Yes Not sure No



YouGov

The Economist / YouGov | June 13 - 16, 2025 • Get the data

Oil prices have been revised down notably, creating budgetary problems for Moscow



Trump's Policy towards Ukraine

Trump's tilt towards Ukraine is becoming more clear, amid a continued lack of pressure on Russia

We remain cautiously optimistic Trump will not abandon Kyiv, and some aid will continue. After extreme pressure on Ukraine earlier this year, relations have improved notably, including with the signing of the US-Ukraine Minerals Deal. Relations with European allies have likewise improved, as evident at the NATO summit in June, though worries persist related to the pending trade war. Meanwhile, Trump has made some rare public criticisms of Putin lately. For these reasons, we also expect the US to enact much tighter sanctions against Russia's oil exports, in unison with the EU.

- **US-Ukraine Minerals Deal:** Particularly compared to earlier proposals of this deal, Ukraine signed in the end a deal that marks a genuine partnership with the US which is already encouraging American businesses to explore investment opportunities in Ukraine. While the financial and economic benefits will take years to realize, more importantly is the political and security aspect of the deal. Ultimately, the deal signifies the US's commitment to Ukraine's long-term independence and sovereignty, while also creating the pathway in this deal for purchasing US military equipment.
- **Joint US-European pressure building:** Following acrimonious relations at the start of the year, US and European relations have improved notably. Far more positive relations have been evident in numerous individual encounters between Trump and European leaders as well as at the NATO Summit in The Hague in June, where Trump was satisfied with European defense commitments and reconfirmed Article 5, which had come under question earlier. Likewise, in line with European rhetoric towards Putin, Trump has also criticized Putin personally for his stalling in talks and indicated a joint sanctions package is possible.
- **US domestic political drivers:** Much of the White House's hesitance to fully support Ukraine is rooted in domestic political reasons, namely an aversion to continue any policy of the previous Democrat administration. Now that Russia's disinterest in peace is becoming abundantly clear to US Congressmen and Senators, as well as much of Trump's administration and Trump himself, we expect policy to move further in support of Ukraine despite the earlier skepticism and hesitance largely driven by antipathy and distrust in any foreign policy conducted by Biden.

Since the Trump-Zelenskyi meeting in The Vatican, US-Ukrainian relations have been on an upward trajectory



Europe and Ukraine

Europe must take care of its own (and Ukraine's) security for the first time in 80 years

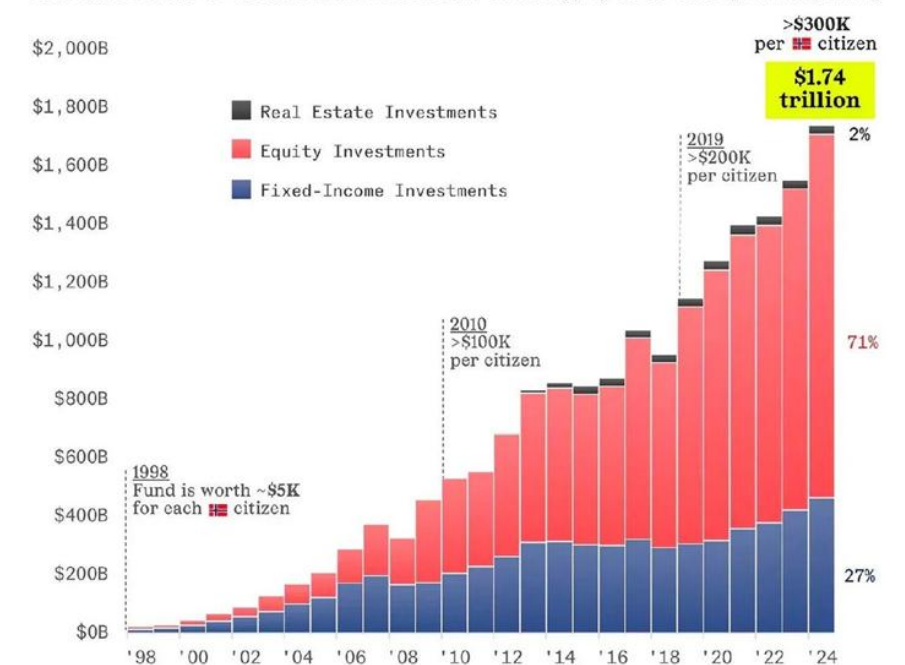
Very positively, Europe is stepping up and filling gaps in US support to Ukraine. Based on both political rhetoric as well as financial actions, Europe understands it must take care of its own security - as well as Ukraine's - for the first time in 80 years. Europe has the financial capacity to provide for its own defense, and now is largely demonstrating the political will. Concerns exist related to dissension within the EU naturally; however, we believe the primal fear over national security will trump any concerns and the EU will "do whatever it takes" to support Ukraine, in the words of German Chancellor Merz.

- **GDP differential:** The total GDP of the EU (~\$20 trn) is 10 times Russia's (\$2 trn), allowing for far greater fiscal space for defense spending. Even at purchasing power parity, Europe's GDP is ~4 times that of Russia's, giving it greater capacity when accounting for Russia's lower production costs. Also, Europe is also able to tap international capital markets, unlike Russia.
- **Defense support to Ukraine:** Nearly every Northern European country, as well as the UK, has raised their defense spending and support to Ukraine significantly in recent months. Notably, Germany and Norway have each increased their support to ~\$8 bn this year, while all NATO members vowed to increase defense spending as a share of GDP to 5% by 2035.
- **EU's €800 bn defense spending package:** The EU announced this package after the Oval Office spat in February. While most of the funding simply allows for hikes in defense spending, funds made available from the COVID recovery and defense loans will drive this.
- **Germany's end of the debt brake:** Critically, Germany – the core of European political and economic power – is squarely leading the defense initiative. In a historic move of exempting defense spending from its fiscal debt brake, Germany is unleashing hundreds of billions of euros towards defense and nearly doubling its aid to Ukraine this year.
- **Norway's Sovereign Wealth Fund:** Major rises in both export volumes and prices of gas to Europe since 2022 has driven Norway's SWF towards \$1.8 trn, earning \$222 bn just in interest in 2024. Pressure is rising both in Norway and the EU for Oslo to tap these funds for defense.

Concerns remain. Pro-Russian actors in Hungary and Slovakia create obstacles towards unified support to Kyiv. However, numerous legal steps, matched with much greater political will, exist to circumvent these countries' obstruction.

Norway's Enormous Wealth Fund Keeps Growing

Total Market Value of the Government Pension Fund of Norway, By Asset Class [\$ billions, annual]



War Tracker

Uncertainty and a prolongation of the war become more likely as ceasefire hopes fade

- **As anticipated, ceasefire talks have effectively broken down.** Putin's total disinterest in a ceasefire has become clear as he retains his maximalist demands. Putin believes he is winning and the West is destined to weaken its support to Ukraine, ensuring a Russian victory over time in Putin's eyes. Meanwhile, Trump's team to date refuses to place pressure on Russia, which is in fact the only way to move towards a ceasefire. With a ceasefire unrealistic in the near term, we believe the likelihood should pick up by early 2026 assuming tougher US and EU sanctions on Russia's oil exports in the coming months. With the current likelihood of a ceasefire low, we have kept our likelihood for a "Frozen Conflict" scenario (*next page*) at a relatively elevated level, where it was prior to Trump's election and his promises to end the fighting.
- **Positively, the EU has clearly stepped up in H1 and is set to provide the required security support to Ukraine in order to bring about peace in the future.** A policy of containment is required to repel Russian aggression, and while until the very recent past the US was that security guarantor, the responsibility for upholding Ukraine's sovereignty as well as Europe's security is now Europe itself. In the event of US abandonment of both Ukraine and Europe – less likely currently than earlier this year – the impact will be notable and unfortunate, but not critical or immediate. The vast majority of Ukraine's military needs are either domestically produced or provided by Europe. Core areas of drones, artillery, ammunition, and mines can be adequately requisitioned to avoid a collapse. Worryingly though,, long-range precision strikes and long-range air defense capabilities would be impacted within months.
- (cont'd) However, particularly following the signing of the US-Ukraine Minerals Deal, US detachment from NATO, European security, and Ukraine look far less likely than earlier. We continue to believe that the US will sell the necessary weaponry to the EU and Ukraine.
- **The battlefield has become more dynamic lately**, as Russia's counteroffensive is underway. Russia has gained territory at a faster pace the past two months than in the previous year, though at a continued extreme loss of manpower. Advances are occurring still on only a few fronts, while the air assaults across Ukraine have picked up to record levels. Related to a potential ceasefire, Ukraine would need to stabilize the front later in the year to provide Ukraine, Europe, and the US greater negotiating power.
- **A strong upside is possible for Ukraine.** As we expect with mild confidence that some US aid will continue, Ukraine's outlook would be much improved, reinforcing our belief in a land-for-peace deal. In this nightmare scenario for Moscow, a robust Ukraine backed by a revitalized Europe and supportive US would ensure the defeat of Russia in the long run.
- **In summary, the most likely scenario remains a land-for-peace deal.** Russia's victory in Ukraine remains unlikely as this scenario is tantamount to a collapse of the Western order, threatening the viability of the EU, NATO, UN, and other Western-created institutions. To stop this, Europe will have to provide the security for itself and for Ukraine, which is entirely feasible financially and militarily, and now necessary politically. With a lower chance of a ceasefire due to the minimal pressure on Russia to date, a prolongation of fighting into 2026 becomes more likely now.

War Tracker

Trump's ineffective diplomacy results in continued fighting, while maintaining the base case of a Ukrainian "victory"

Russia-Ukraine War Scenarios into 2026

End point	Scenario 1: Russian 'victory' (Collapse of Western Order)	Scenario 2: Ukraine 'wins', Land-for-Peace Deal	Scenario 3: Frozen conflict, fighting persists at lower level	Scenario 4: Direct Russia-NATO confrontation
Likelihood	10% (was 20%)	60% (was 50%)	25% (was 15%)	5% (was 15%)
Timeline	H2 2025	H1 2026 at earliest	Late-2025	Through 2025 and beyond
What it looks like	<ul style="list-style-type: none">• Trump cuts off US support• Europe cannot provide adequate support• Kyiv forced to negotiate a bad peace• Russia seizes far more land• Ukraine turns war into an insurgency	<ul style="list-style-type: none">• Neither side can shift the line of contact decisively• Russia seeks a ceasefire to pause the war• Zelenskyi offers land-for-peace• West provides more aid and security guarantees	<ul style="list-style-type: none">• Neither side can strategically shift the war in its favor• Western aid to Ukraine moderates• Kyiv is forced to negotiate, while Moscow declares a "victory"• The two sides get stuck in extended negotiations and fighting persists	<ul style="list-style-type: none">• NATO-Russian War instigated by a Russian attack on a NATO country or tactical nuclear strike in Ukraine• The West responds with an overwhelming conventional response• Potential for Russian nuclear retaliation in the West

Russia's 2025 Economic Outlook

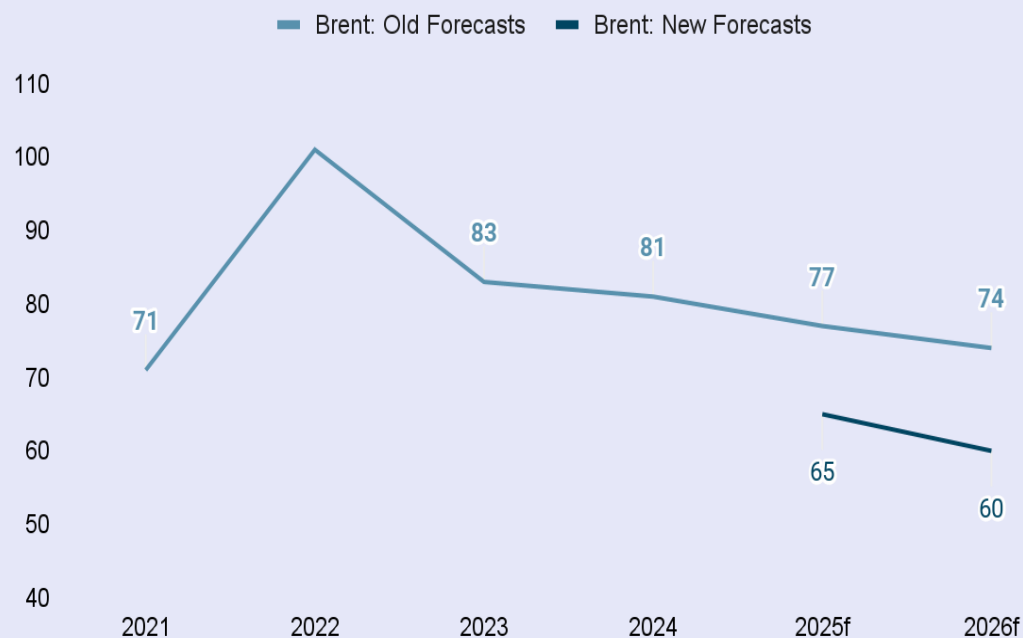
The Kremlin will likely seek to pause or slow the war by early 2026 to avoid an economic crisis

- **Pressure on the Russian economy remains high and will continue to worsen.** GDP performed well across 2024, though signs of clear weakness appeared in 2025. In Q1, the Russian economy fell by 0.6% in quarter-on-quarter terms amid a 10% drop in oil revenues, and is expected to decline in Q2 as well, marking a technical recession in H1. The economy has effectively not grown since late 2023, but rather has simply risen in year-on-year terms for most of 2024 (stagnating in month-on-month terms). Assuming now much lower oil prices (low \$60s) this year, GDP would likely contract mildly amid coming sharp ruble depreciation, accelerating inflation, and debilitatingly high interest rates.
- **The corporate sector has seen problems arise, impacting investment potential.** A sharp rise in preferential lending to defense firms caused a 71% increase in corporate borrowing since mid-2022, amounting to a level of 19% of GDP (\$415 bn). Repayment of these loans will be costly and demand state support. Compounding matters, energy exporters have seen declining revenue since late 2024 and will face greater pressure in the months ahead.
- **Meanwhile, oil prices have moderated notably in H1**, and will face further pressure amid a supply surplus from rising OPEC and US output as well as lower demand from a weakening US economy. Brent crude oil prices are forecast to average \$65 in 2025 given weaker global growth from the tariff wars. However, an exacerbation of the Israel-Iran war could push prices up.
- **The Russian budget has been amended to account for a much higher deficit (1.7% of GDP).** Moscow now expects a a \$15 bn drop in revenues amid spending hikes for defense, has cut some non-defense spending, and has lowered the budgeted oil price from \$70 to \$56. Russia sells its oil ~\$10 less than the Brent crude price (currently mid-\$60s), so Russia is now selling oil at around the adjusted budgeted oil price. With state spending up 21% YOY in Q1, the deficit has expanded, hitting 1.5% of GDP while state support the civilian economy contracts. As long as the war continues, extreme defense spending and imports to sustain defense manufacturing will continue, driving high inflation and interest rates into 2026. Wages – up 10% YOY in Q1, after averaging 18% in 2024 – will remain elevated given the severe shortages of labor resulting from military recruitment, further driving up inflation (averaging 10% Jan.-May) and interest rates (20% currently). Investment is set for a marked slowdown in 2025, particularly amid the rise in the corporate tax rate.
- **Assuming tougher Western sanctions, by early 2026, the Kremlin will become increasingly interested in a ceasefire/operational pause** due to rising pressures. Continuous removal of manpower from the labor market to the war matched with falling budget revenues will threaten macroeconomic stability by early 2026, impacting Moscow's ability to continue to prosecute the war. Meanwhile, high interest rates hurt the domestic bond market, creating problems in funding a rising budget deficit.

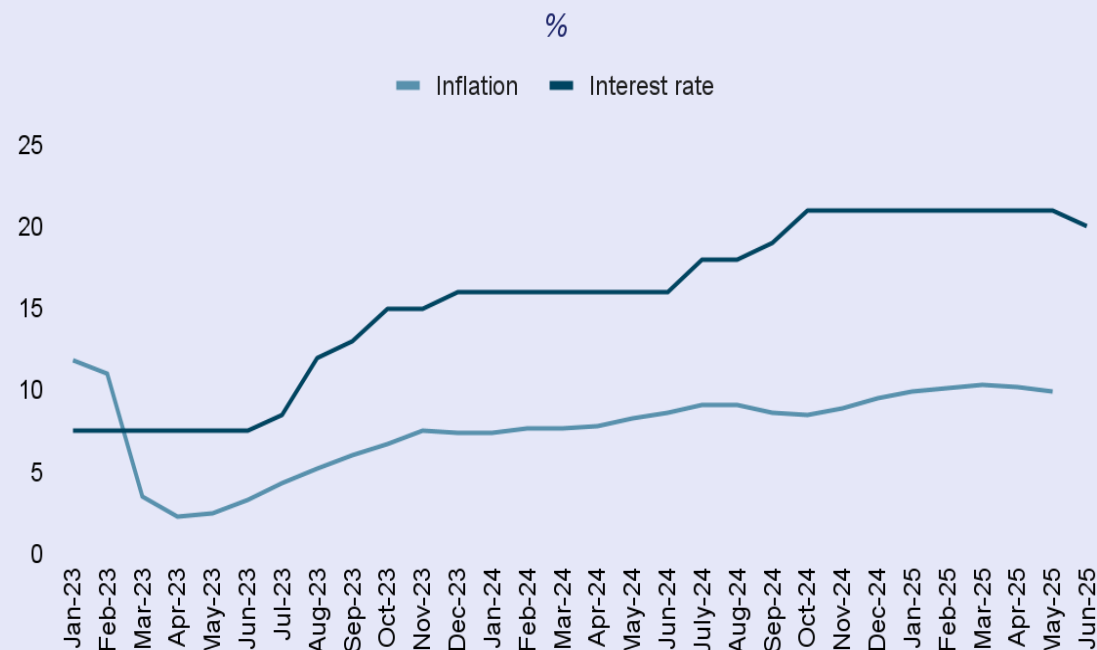
Russia's 2025 Economic Outlook

The Kremlin will likely seek to pause or slow the war by early 2026 to avoid an economic crisis

Oil prices have been revised down notably, creating budgetary problems for Moscow



High labor costs and food prices ensure high inflation and interest rates in 2025, creating the conditions for a crisis



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