from Ukraine, domestic prices for many products are set according to global conditions which means that the cost of energy and food have risen significantly as a result of the conflict, even though the UK does not depend directly on many supply chains from Ukraine. The UK's supply chain issues arose from global shortages of materials, staff shortages and transport delays which were occurring at the same time as sharp spikes in demand, particularly for consumer goods and construction materials. The conflict in Ukraine has added to food supply chain pressures, particularly in relation to rising costs for fertilizers, animal feed and energy. The UK Government expects further food price increase due to trade disruptions and fertilizers supply issues. Farmers in the UK have concerns about the input costs, particularly fertilizers and animal feeds, as well as energy costs. Sanctions on Russia are already starting to worsen an acute cost of living crisis in the UK. Although limited dependence on Russian imports, surging global prices are expected to erode the living standards even further. Olly Bartrum, a senior economist at the Institute for Government (IfG), said that disruptions in the global metal markets will affect many key UK sectors like automotive, smartphones and aerospace. According to the Office for National Statistics, the UK's debt interest bills have already hit their highest level in January 2022. The UK imported no fuel from Russia in June 2022 for the first time on record, according to official figures. It has pledged to phase out Russian oil imports by the end of the year 2022 and gas imports as soon as possible. The effects of Brexit on labor markets including added paperwork and border frictions for imports, have left the UK vulnerable to pre-existing supply-side issues. The domestic labor market has also been baffled due to large changes in supply and demand from the pandemic or Brexit. The UK began the year 2022 with a record of 1.3 million vacancies and an increasingly tight labor market.

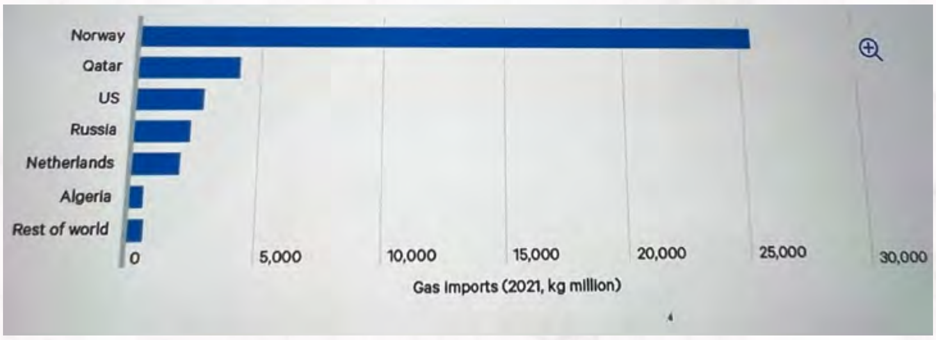
Objective:-

The objective of this paper is to find out the impact and vulnerability of the war between Russia and Ukraine on the UK economy with the help of data collected.

Data Source:-

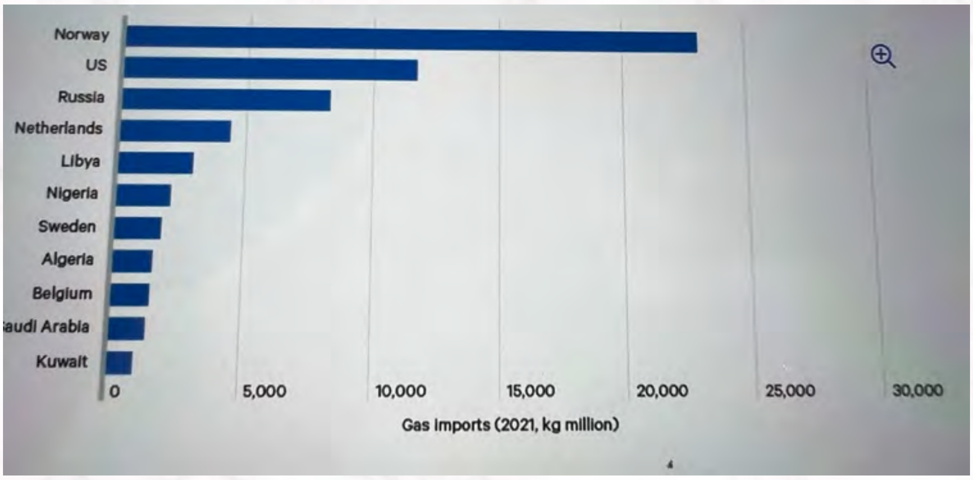
The UK ranks far below other European countries in terms of reliance on gas imports from Russia. Just 3% of the UK's gas imports comes from Russia. A Russian embargo would not turn off the taps for UK households, however such an event could have a knock-on effect for availability of gas from the UK's main supplier, Norway.

Fig1:- UK gas imports by source,2021



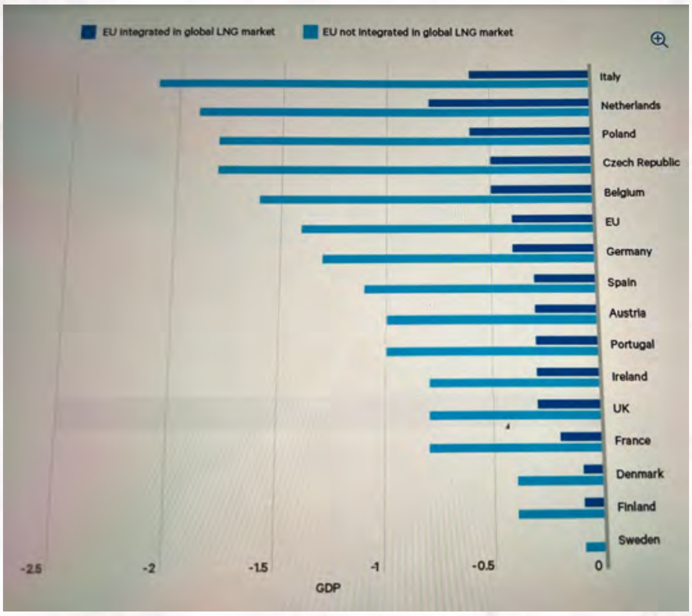
Source:- HM Government(undated), 'UK Trade Info'

Fig2:- UK oil imports by source, 2021



Source:- HM Government(undated), 'UK Trade Info'

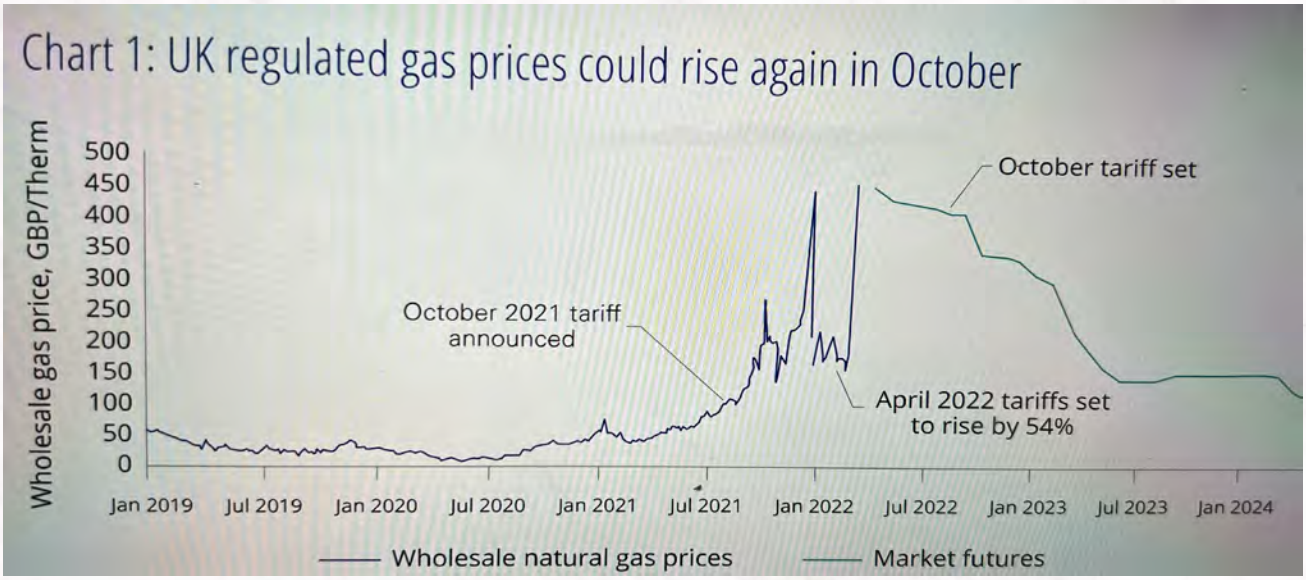
Fig3:- GDP impact of Russia cutting gas supplies to Europe



Source:- Di Bella, et al. (2002), 'Natural Gas in Europe: The Potential Impact of Disruptions to Supply', International Monetary Fund, July 2022

Although Russia and Ukraine together represent one-quarter of global wheat exports and about 15% of corn and fertilizer exports, it does not affect the food security of the UK as it stands in a relatively strong position. However, the UK's comparatively strong position does not immune it to inflationary pressure caused by reduced global supply. Since the UK is fully integrated into global markets for both energy and food, British households face higher prices for both commodities. The higher price of wheat alone is up by more than 50%as of 7 March 2022 which could add more than one percentage point to UK inflation. On the other hand, higher global market prices benefit the UK energy industry overall as some UK-based energy firms have posted large profits in 2022 but this secure energy supply does not necessarily mean cheap energy for UK consumers. Due to the UK energy price cap and increased demand, the most expected impact will be on consumer prices in late 2022 or early 2023. The price cap could even exceed 4000 pounds a year for an average domestic consumer- taking a significant proportion of most UK household's disposable income. The price of wheat which was a major Ukrainian export has risen 40% since the start of the war. Areas which were having cost-push inflation have had a knock-on effect on UK prices. France and Southern Europe from which the UK imports much of its food was under pressure from global price rise. The UK's financial links to Russia poses moral and political problems but they do not constitute a major part of British trade and inward investment as in 2020, it received 681 million pounds FDI from Russia which was less than 0.1% of the total UK inward FDI stock and a small sum compared to the 11.2 billion pounds of British FDI in Russia. Global oil prices have increased by 11% and the UK wholesale gas prices have increased by 40% since the invasion. In March, the UK consumer confidence fell to its lowest level since November 2020. Energy prices were increasing before the war in Ukraine but as a net importer, the UK is exposed to volatility in the price of gas. Energy input costs for farms increased by 34% between January and April 2022. Also the price of farm fuel cost increased by 30% over the same time.

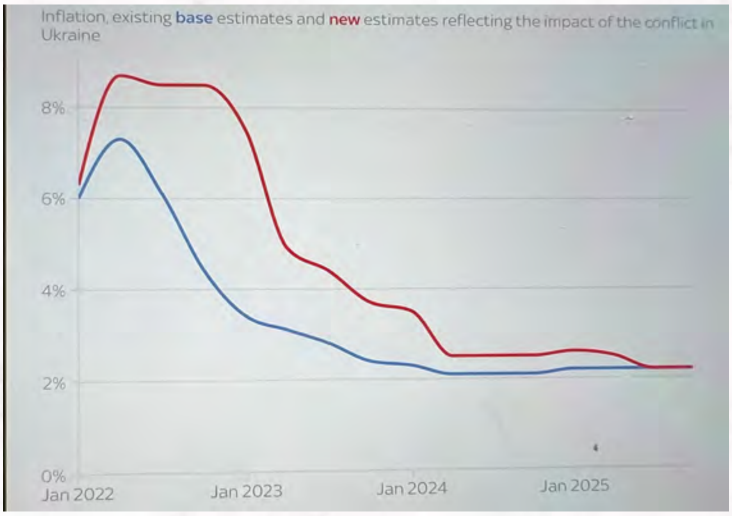
Fig 4:-



Source:- Refnitiv Eikon, KPMG Analysis, 7 March 2022

According to the Centre for Economic and Business Research (CEBR), the average UK household will experience a 2553 pounds drop in income in 2022 half of which is due to the results of the war. It also estimated that living standards in the UK will drop at the worst rate since records began in the mid-1950s. CEBR stated worryingly that the cost of living will stay above seven percent till the beginning of 2023, resulting in the UK economy posting zero growth over the whole of 2023. The invasion of Ukraine will lead to a noticeable increase in the cost of living in the UK as depicted in the figure below.

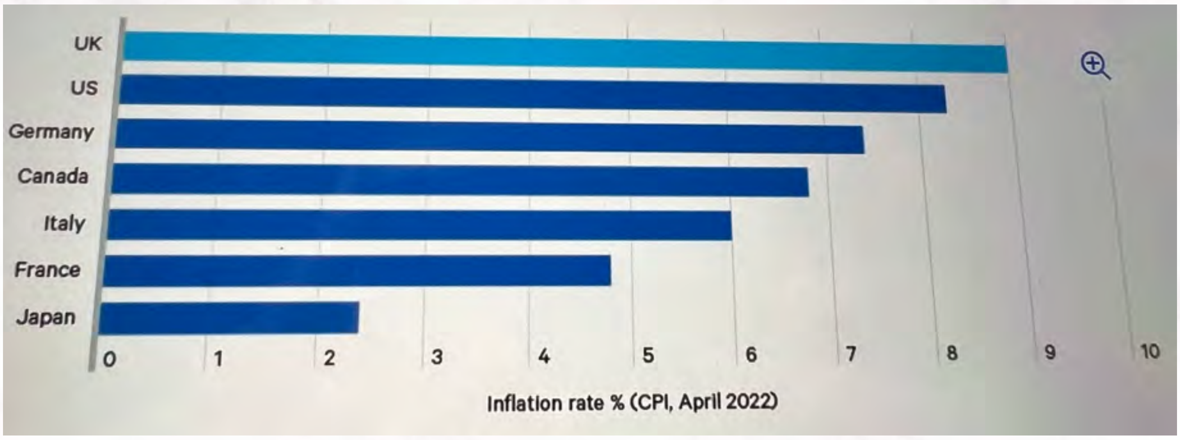
Fig 5:- Impact of the invasion on inflation



Source:- CEBR

As a services economy, the UK imports few raw materials but a huge number of manufactured goods, which have now become more expensive due to the increased cost of input prices. The effects of Brexit on labor markets have left the UK vulnerable to rising inflation. The war had just added extra pressure to the pre-existing supply side issues. Due to all of these factors the UK has the highest rate of inflation in the G7 as depicted in the figure below.

Fig 6:- Inflation rate among G7 members



Source:- Institute of Chartered Accountants in England and Wales (2022), 'Chart of the week: Inflation around the world', 26 May 2022

Russia's war with Ukraine will deal a blow of 90 billion pounds to the UK economy driven by a worsening cost of living crunch sending the British consumers into retreat. A ratcheting up in the cost of living will deliver a 2550 pounds to each household in Britain. A combination of rampant inflation and steep tax hikes has caused the households to face a once-in-e-a-generation hit to their standard of living. The households' budgets had pulled back their consumer spending which generated around 60% of output in the UK are now squeezed causing a shave over two percentage points off economic growth in 2022. In 2021 the cost of gas was 40p per therm which has now become 8 pounds per therm due to US and European countries mulling banning imports of Russian energy.

Despite limitations over trade, some parts of the UK economy are well reliant on Russia. According to UN Comtrade data, the UK gets almost 20% of their vegetables from Russia. Fuel imports from Russia fell by 499 million pounds or 100% compared with the average for the previous 12 months to February. Exports of most goods to Russia had decreased substantially by June 2022 overall by 70%or 168 million pounds, with machinery and transport equipment sales slashed by 91.3% or 118 million pounds.

Fig 7:- How much UK trade is affected by the war?

Source:- UN Comtrade

Conclusion:-

In the long run, Russia's invasion of Ukraine would likely encourage a recent trend towards de-globalization, with supply chains becoming increasingly fractured and politicized. Countries like the UK, who rely on imports of energy, food and manufactured goods, are becoming keen to establish diverse and trusted supply chains with like-minded partners. This is basically a part of insurance policy against geopolitical risks such as the war in Ukraine but also partly as a response to domestic political demands.

A more substantial impact is to come from the introduction of new sanctions like:-

- Direct effect on investment and business activity in the UK through legal restrictions
- Indirectly affect trade and investment through the perception that the UK is no longer open to business in certain sectors or with certain kinds of companies and individuals
- Affect future business activity through setting a precedent of applying sanctions against unsavoury regimes

Due to the war, British major companies like Marks & Spencer's and Vodafone, have shut down their operations in Russia or cut ties with partners in the country, largely as result of consumer pressure and public relations concerns, rather than the legal requirement of international sanctions. Also the British economy is forecasted to slow to a standstill in 2023 as it suffers more than any other major industrial countries due to war. According to the Paris-based think tank the Organisation for Economic Co-Operation and Development(OECD), the UK is expected to grow by 3.6% in 2022 before posting zero growth in 2023 with an average expected inflation of 8.8% in 2022 and fall only slightly to 7.4% in 2023. The think tank's chief economist said that the UK was being hit by a combination of factors, including higher interest rates, higher taxes, etc.

Reduced trade and more expensive energy. The invasion of Ukraine has further raised the prospects of stagflation which is going to affect the UK economy in particular, worsening the squeeze on household incomes. However the conflict has led experts to warn Brits will absorb one of the harshest blows to their finances in peacetime.

The Government of the UK has published a Government Food Strategy for England on 13 June 2022 in response to the invasion of Ukraine which includes following outlined actions to be taken

- setting up a package on fertilizers to help the farmers manage their increased input costs
- Future work with industry on barriers to farmers taking up risk management and other farming insurance products
- Access to more diverse supply chains where there were shortages of ingredients and helping businesses to manage vegetable oil substitutions
- strengthening the resilience of domestic supply chain

It is expected that there will be a considerable jump in the prices the UK citizens pay at the supermarket and petrol pump. If gas and electricity prices stay at the current levels, the Resolution Foundation predicts that the energy price cap in next winter would be almost 1000 pounds higher than the elevated level set to be introduced in April (1971 pounds). The CEBR has predicted that inflation will now peak at 8.7% next quarter and then stray twice as high as expected until the second half of 2023 which means that suppose a shopping basket which cost 20 pounds a year ago will now cost almost 22 pounds in the next few months. If their forecasts materialize then a large portion of the UK's stock of debt would rise in line with the retail price index which means that the government's debt interest bill will swell which was already at its highest level ever in January 2022. Hence as said by Yale Self-indulgent, chief economist at KPMG UK, the ongoing squeeze on household finances continued to weigh on growth and likely to have caused the UK economy to enter a technical recession from the third quarter of 2022.

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