Economists discuss the economic fallout of Russia's war in Ukraine

*What are the likely economic consequences of Russia's invasion of Ukraine and the responses by the international community? The Initiative on Global Markets surveyed US and European economists in top universities, including LSE's **Christopher Pissarides** and **Ricardo Reis**. They express their views on the potential fallout for the Russian economy, the European economy, the US dollar's role as an international currency, and global growth and inflation. **Romesh Vaitilingam** sums up their views.*

The Initiative on Global Markets asked their US and EU panels whether they agreed or disagreed with four statements, and, if so, how strongly and with what degree of confidence. Of the 43 US experts, 40 participated in this survey; of 48 European experts, 41 participated – for a total of 81 expert reactions.

Statement 1. The fallout from the Russian invasion of Ukraine will be stagflationary in that it will noticeably reduce global growth and raise global inflation over the next year.

More than three-quarters of the panel agree with this statement, and the rest are uncertain.

Weighted by each expert's confidence in their response, 16% of the US panel strongly agree, 65% agree, 19% are uncertain, and 0% disagree or strongly disagree. Among the European panel (again weighted by each expert's confidence in their response), 34% strongly agree, 44% agree, 22% are uncertain, and 0% disagree or strongly disagree.

Overall, across both panels, 26% strongly agree, 53% agree, 21% are uncertain, and no one disagrees.

Among the short comments that the experts are able to include in their responses, **Karl Whelan** at University College Dublin, who strongly agrees, says: 'This is a classic negative supply shock. As we know from the 1970s, these shocks raise inflation and reduce output.' **Robert Shimer** at Chicago, who says he is uncertain, accepts the diagnosis but not necessarily the outcome: 'It's an adverse supply shock. Whether that is inflationary depends on the monetary policy response.' **Larry Samuelson** at Yale, who agrees with the statement, comments: 'A protracted conflict, on top of existing supply-chain woes, will be detrimental to the world economy.'

Others who agree point to the likely drivers of lower growth and higher inflation. **Christopher Pissarides** at the London School of Economics and Political Science (LSE) explains: 'The effect will be through oil and other resources. Supply will be reduced so prices and production costs will rise.' **Franklin Allen** at Imperial College London notes: 'The invasion is affecting inflation already with oil, gas and many other commodities reaching high levels. Output may also fall.' **Markus Brunnermeier** at Princeton adds: 'Russian economy is not large, but the increase in energy prices will have adverse effects on several emerging markets and the European Union'. And **Anil Kashyap** at Chicago mentions: 'Lots of disruptions, energy, neon, palladium (both important for chips), wheat.'

Among those who say that they are uncertain, **Antoinette Schoar** at MIT remarks: 'There will surely be large economic repercussions, but I am not entirely sure that it will be stagflation.' **Olivier Blanchard** at the Peterson Institute states: 'I am reasonably confident about inflation, but less sure about output. Demand may be strong for other reasons.' And **Eric Maskin** at Harvard observes: 'Stagflation seems a plausible outcome, but I wouldn't want to make a point prediction that it will happen.'

Others who are uncertain explain why. **Kjetil Storesletten** at the University of Oslo replies: 'Russian inflation will reduce world growth. Unclear what it will do to inflation.' And **Jan-Pieter Krahnen** at Goethe University Frankfurt comments: 'Consequences of the war go both ways: supply chain and energy prices lower growth; energy substitution and military buildup do the opposite.'

Statement 2. The economic and financial sanctions already implemented will lead to a deep recession in Russia.

On this statement, over 90% of the panellists agree and again none disagree.

Weighted by each expert's confidence in their response, 16% of the US panel agree, 77% agree, 8% are uncertain, and 0% disagree or strongly disagree (totals don't always sum to 100 because of rounding). Among the European panel (again weighted by each expert's confidence in their response), 45% strongly agree, 49% agree, 6% are uncertain, and 0% disagree or strongly disagree. Overall, across both panels, 32% strongly agree, 61% agree, 7% are uncertain, and none disagree.

Comments from those who agree include **Larry Samuelson**, who says: 'One already sees signs of disruption, though it is less clear that the effect will be a deep recession.' **Karl Whelan** notes: 'Russia runs a large non-energy current account deficit. Loss of access to supplies and services will hurt the economy.' **Jan-Pieter Krahnen** suggests: 'While I expect to see a recession because of global pull out from Russia, there are also some counter effects from rising energy revenues.' **Franklin Allen** adds: 'There is uncertainty about how effective sanctions will be and how much China will help avoid them. But it seems likely output will fall.'

Some panellists who agree note the significance of the coverage of sanctions and the length of time that they may be in place. **Kenneth Judd** at Stanford declares: 'Yes, IF we maintain them. We cannot retreat. We must maintain this united squeeze on Putin.' **Daron Acemoglu** at MIT says: 'Yes, but recall that they are not fully comprehensive (yet). The West should halt all gas imports and exclude all Russian banks from Swift.' **Christopher Udry** at Northwestern adds: 'But stronger sanctions are still available and should be implemented.'

Among those who say they are uncertain, **Markus Brunnermeier** notes: 'Growth was already low beforehand in Russia. Sanctions will take time to work.' **Patrick Honohan** at Trinity College Dublin states: 'Gas/oil exports can still pay for Russia's imports. Recession more likely to be driven by collapse of domestic confidence.' **Christopher Pissarides** says: 'For as long as Russia can sell its oil it will have the revenue. It can then trade with Asia. But switching markets will be costly.' And **Robert Hall** at Stanford observes: 'Imposing autarky does not necessarily lower activity.'

Statement 3. Targeting the Russian economy through a total ban on oil and gas imports carries a high risk of recession in European economies.

On this third statement, 70% agree, and most of the rest are uncertain. It is worth noting that there are considerably stronger expectations of a recession among the European panel. At the same time, several panellists express the view that even if an energy embargo were to be costly for Europe's economies, it may still be desirable to implement one.

Weighted by each expert's confidence in their response, 19% of the US panel strongly agree, 42% agree, 40% are uncertain, and 0% disagree or strongly disagree. Among the European panel (again weighted by each expert's confidence in their response), 16% strongly agree, 61% agree, 19% are uncertain, and 3% disagree.

Overall, across both panels, 17% strongly agree, 53% agree, 27% are uncertain, and 2% disagree.

Among those who agree or strongly agree, **Luigi Guiso** at the Einaudi Institute for Economics and Finance notes: 'Europe is heavily dependent on Russian gas, substituting it takes substantial time'. **Christopher Pissarides** concurs: 'Germany is totally dependent on them. A recession in it and some others will bring recession to Europe.' Similarly, **Lubos Pastor** at Chicago points out that: 'Several large European economies, including Italy and Germany, are highly dependent on Russian gas.' And **Jose Scheinkman** at Columbia explains: 'Recessionary effect will come mostly from banning gas imports, since the effect from oil will be partially diluted by reshuffling supplies.'

Others who agree about the costs to Europe of an embargo recognize that it may still be warranted. **Jan-Pieter Krahnen** argues: 'Unfortunately, yes. I would nevertheless advocate closing Nord Stream 1, the existing gas pipeline, and to substitute via renewables.' **Barry Eichengreen** at Berkeley says: 'Note that this is not necessarily an argument against such a ban.' And **Ricardo Reis** at the London School of Economics concludes: 'But it is worth it.'

Some of those who are uncertain take a similar line. **Christian Leuz** at Chicago states: 'Possible but hard to know. It should still be considered for political and humanitarian reasons. It might be a price worth paying.' And **Anil Kashyap** comments: 'Probably? But doubt we won't try, and hard to gauge how much substitution is possible. Continued purchases are helping with foreign exchange for Russia.'

Others who are uncertain acknowledge the downsides but are not sure that they will lead to recession in Europe. **Daron Acemoglu** says: 'Of course, it will be more costly for Europe, but not clear whether it will push them into severe recession.' **Jean-Pierre Danthine** at the Paris School of Economics suggests: 'Would clearly lead to a slowdown, possibly recession in some more dependent economies.' And **Karl Whelan** responds: 'Unsure. It is a negative factor but the recovery from the pandemic has been strong and household balance sheets are in good shape.'

Still others comment on potential shifts in the global energy market, **Franklin Allen** says: 'Difficult to say at this stage as it may simply be that total supply remains the same and which countries supply Europe changes.' And **Kenneth Judd** argues that: 'We need to get OPEC to increase supplies and change some US policies to increase flow of oil to Europe.'

Jan Eeckhout at Universitat Pompeu Fabra Barcelona disagrees with the statement, noting: 'There will be transition, but eventually Russian oil/gas will be consumed somewhere (China, India…) if not in Europe.'

Statement 4. Weaponising dollar finance is likely to lead to a significant shift away from the dollar as the dominant international currency.

On the fourth statement, reactions are much more mixed than on any of the other questions.

Weighted by each expert's confidence in their response, 24% of the US panel agree, 40% are uncertain, 32% disagree, and 5% strongly disagree. Among the European panel (again weighted by each expert's confidence in their response), 23% agree, 33% are uncertain, 39% disagree, and 4% strongly disagree.

Overall, across both panels, 24% agree, 36% are uncertain, 36% disagree, and 5% strongly disagree.

Among those who agree, **Jan-Pieter Krahnen** claims: 'This shift away from the dollar is under way already, as weaponizing of finance has become an element in international politics for years.' **Robert Shimer** remarks: 'More true for countries like Russia and China that may fear future sanctions.' And **Christopher Udry** makes a comment similar to those about an energy embargo being costly for Europe but nevertheless worthwhile: 'Although I am not sure about the "significant". In any case, a price that is worth paying.'

Others who agree suggest potential alternatives to the dollar. **Darrell Duffie** at Stanford comments: 'With weaponization of dollar payments, workarounds would move moderately toward cryptocurrencies and other payment arrangements.' **Lubos Pastor** adds: 'Gold, crypto, and renminbi are likely to gain market share at the expense of western currencies such as the dollar.' **Jose Scheinkman** cautions: 'But since measures also involved the euro, the yen, sterling and the Swiss franc, countries planning to invade democracies would be restricted to gold, crypto or renminbi.'

Among those who say they are uncertain, **Maurice Obstfeld** at Berkeley comments: 'Not if it is only in cases like Russia now.' **Franklin Allen** explains: 'Maybe in the long run the role of the dollar will fall, but in the short to medium term network externalities may dominate.' **Jean-Pierre Danthine** states: 'The dollar will remain the (somewhat less) dominant international currency.' And **Abhijit Banerjee** at MIT argues that: 'All the forces that could lead to a move away from the dollar were already there. But maybe this could act as a sunspot.'

Several panellists who disagree that the dollar will be diminished in status point to the size of Russia's economy. **Kjetil Storesletten** says: 'While Russia might try to rely less on dollars, the dollar's dominant role will remain. Russia is too small.' **Pol Antras** at Harvard concurs: 'Russia's economy is small. Need to see China's ultimate reaction, though.' And **Pete Klenow** at Stanford links to recent data on the Russian share of world GDP and trade: 1-2%.

Others who disagree draw attention to the absence of realistic alternatives to the dollar, some focusing specifically on China and its currency. **Charles Wyplosz** at the Graduate Institute, Geneva, asks: 'Away from the dollar into what? Not renminbi, which is not really fully convertible.' **Daron Acemoglu** adds: 'What's the alternative? Renminbi? It can be argued that China has ruined its international standing with its full-throated support for Russia.' **Patrick Honohan** notes: 'This is not the first time dollar has been weaponized. And financial sanctions are not just by the US. The renminbi still has a long way to go.' **Kenneth Judd** argues that: 'This use of dollar power is supported by all our friends. It would be difficult for China to end its use of the dollar.'

Finally, some panellists are doubtful about the prospects for any alternatives. **Anil Kashyap** comments: 'Highly unlikely in the short run, and the dollar remains "the cleanest dirty shirt". What is the alternative? Doubt it will be crypto!' **Ricardo Reis** at LSE directs us to his research showing that: 'It is hard to jumpstart alternatives, and then to make them grow.' And **Richard Portes** at London Business School concludes emphatically: 'No serious alternative.'

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Notes:

- *The survey is conducted regularly on different topics by The Initiative on Global Markets, of the University of Chicago Booth School of Business. All comments made by the experts are in the full survey results for the US and European panels.*
- *The post represents the views of its author(s), not the position of LSE Business Review or the London School of Economics.*
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