

# Brexit

**Revisited**

presentation by  
**Richard Harris**  
13<sup>th</sup> November 2017

# Overview

- Where are we now in Article 50 negotiations
  - EU position on its two-stage approach
  - UK's preferred position on trade/customs (stage 2)
- Some current major issues
  - UK ignoring complexity on trade/customs?
  - EU/other countries lining up for Free Trade deals?
  - Political instability & uncertainty in UK
  - Importance of trade to UK (but especially services)
- Post-Brexit future for the UK
  - Is UK well-placed to benefit from desired FT position?
  - Will it be a 'hard' or 'soft' Brexit and implications
- Post-Brexit future for New Zealand
  - Does it matter much what is the outcome?

# Where are we now?



- Article 50 invoked end March 2017
  - UK leaves the EU end of March 2019
- EU has a two-stage approach:
  1. ‘Divorce’ settlement; Northern Ireland Border; EU citizens rights 
  2. Trade and Customs arrangements but only after (1) is concluded
- UK are stalling on (1) – mostly ‘divorce bill’ – and pushing hard for start of stage 2
- UK’s preferred position 

# EU stage 1: Divorce Bill



- ‘divorce’ settlement
  - In 2015 UK paid £19.5 billion gross;
    - with rebate (Mrs. T) and structural funding/subsidy spending in UK, net contribution was £14.6bn.
  - Reported that EU opening position is total of €99.6bn gross:
    - €86.4bn for commitments made as a member state for 2014-20
    - €11.5bn contingent liabilities
  - But net bill likely €60.2bn
  - FT thinks:
    - the EU is looking for Britain to cover at least its commitments under the long-term budget... **That would take the total to €64bn in gross terms and €40bn net.** But while such figures would probably be enough for Brussels, they could prove deadly in Westminster.
  - Prime Minister (Florence Speech, September) stated:
    - I do not want our partners to fear that they will need to pay more or receive less over the remainder of the current budget plan as a result of our decision to leave. The UK will honour commitments we have made during the period of our membership.
  - Liam Fox (SoS International Trade) argues we cannot agree a sum until we know what the final deal (including trade) will look like

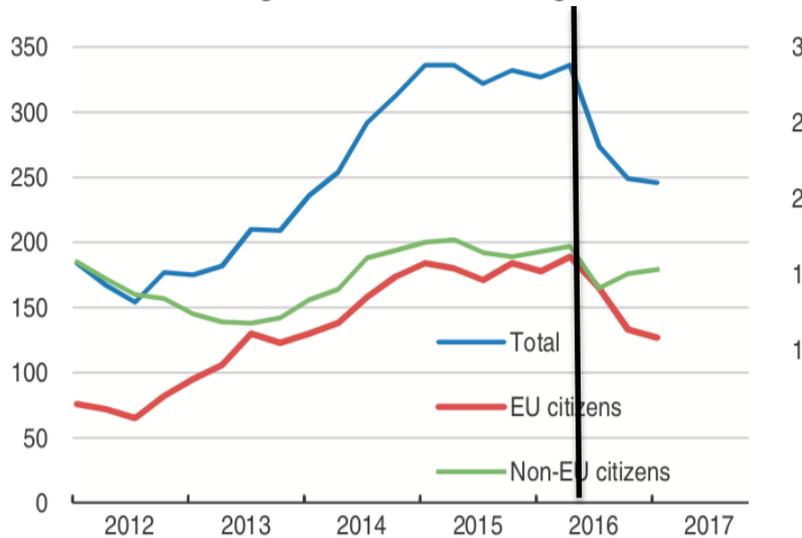
# EU stage 1: NI-Irish border



- EU wants no customs border with RoI
  - Every day 13,000 commercial vehicles cross Irish border; 91,000 Irish companies trade with UK
  - In 2015 Irish imported/exported €17.8/15.5bn with UK (trade was 122% of GDP in 2016 with UK second biggest partner)
- Consequences of customs reintroduced are:
  - 800% increase in customs declarations
  - Ports/airports would need new infrastructure
  - Revenue/customs staff need large increase in staffing
- UK government's position:
  - maintain the Common Travel Area and the rights of UK and Irish citizens, and to uphold the 1998 Good Friday Agreement
  - arguing for a wide-ranging exemption under which small and medium-sized businesses will not have to comply with any new customs tariffs.

# EU stage 1: EU citizens

A. Net migration to the United Kingdom<sup>1</sup>

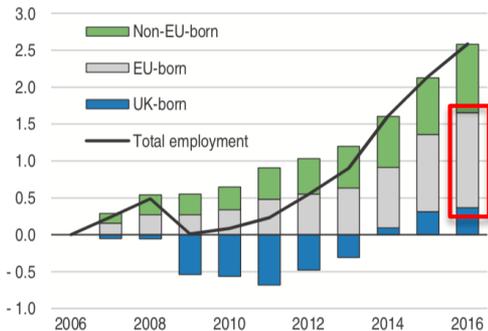


- to the 600,000 Italians in the UK – and indeed to all EU citizens who have made their lives in our country – that we want you to stay; we value you; and we thank you for your contribution to our national life – and it has been, and remains, one of my first goals in this negotiation to ensure that you can carry on living your lives as before

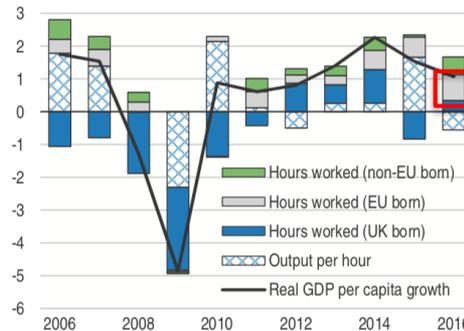
Teresa May (Sept 2017)

1. Net migration is the difference between immigration and emigration

A. Contributions to the change in total employment by country of birth  
In millions



B. Contributions to real GDP per capita growth  
Percentage points<sup>1</sup>



1. Data for hours worked by country of birth refers to hours worked per capita and it is calculated based on employment shares by country of birth.



# UK position



- UK has chosen to:
  - Leave Single Market & Customs Union
    - CU: would prevent UK from negotiating own trade agreements with non-EU27; CU would also not cover trade in services (where non-tariff barriers are high)
    - SM: to regain control over law-making and migration, and avoid budget payments
  - Wants instead to agree with the EU:
    - a Free Trade Agreement
    - Minimalist customs arrangements
    - Agree a transition period of perhaps 2 years (or whatever it takes?) to allow it to negotiate FTA and minimalist customs
      - During period accede to all current obligations
      - BUT as previous Deputy-PM (Clegg) notes (FT 3 October):

How is the UK supposed to stay “in” the legal framework of the EU if we have legally passed the point of no return at the end of March 2019? What happens when new EU rules are produced during the two-year period? What happens if another member state seeks to take the UK to the EU court in Luxembourg? Do we end up obeying EU judges after we have legally left the EU, after all?

# UK position: Free trade



“there is no need to impose tariffs where we have none now, and I don’t think anyone sensible is contemplating this” (Teresa May, September 2017)

- Similar in principle to the Single Market but without freedom of movement of people/capital, and regulation done in UK
  - EU already has some 40 FTA with 53 non-EU countries
  - However does not cover services (which requires ‘passport’ system to ensure regulatory requirements are met)
  - FTA would still require UK to meet EU regulatory and competitiveness laws, so issue of adopting EU laws and dispute resolution (who ECJ and/or UK courts?)
  - Unlikely to conclude by March 2019
    - EU-Canadian FTA took over 8 years to conclude
    - However UK starts from position of full compliance

# UK position: Customs



Either/or (both?)

- **A highly streamlined customs arrangement** between the UK and the EU, streamlining and simplifying requirements, leaving as few additional requirements on EU trade as possible. This would aim to: continue some of the existing arrangements between the UK and the EU; put in place new negotiated and potentially unilateral facilitations to reduce and remove barriers to trade; and implement technology-based solutions to make it easier to comply with customs procedures. This approach involves utilising the UK's existing tried and trusted third country processes for UK-EU trade, building on EU and international precedents, and developing new innovative facilitations to deliver as frictionless a customs border as possible.
- **A new customs partnership with the EU**, aligning our approach to the customs border in a way that removes the need for a UK-EU customs border. One potential approach would involve the UK mirroring the EU's requirements for imports from the rest of the world where their final destination is the EU. This is of course unprecedented as an approach and could be challenging to implement and we will look to explore the principles of this with business and the EU.
- **Summary: try to make trade in goods much as it is now**
  - Mirroring EU customs approach for EU-UK trade
  - Major technological and legal challenges to face
  - Does not cover services and regulatory issues



**Guy Verhofstadt** ✓  
@GuyVerhofstadt



To be in & out of the Customs Union & "invisible borders" is a fantasy.

11:56 AM - Aug 15, 2017

656 2,870 4,212

# Some current major issues



- UK ignoring complexity on trade/customs?
  - For example:
    - » Customs arrangements are costly (cf. rules of origin)
    - » Non-EU firms do not have passporting rights in financial services
    - » Only airlines that are majority owned by EU nationals can operate flights with the EU; UK lorry drivers not licensed to drive vehicles in EU
    - » Most existing EU trade deals (e.g., EU-Canada) do much less than Single Market to harmonise economic regulation and they do not guarantee market access for service providers
  - Why should EU be a willing partner in such arrangements?
    - » EU's approach to Brexit negotiations is:
      - A country outside the EU that does not live up to the same obligations as a member, cannot have the same rights and enjoy the same benefits as a member (European Council, 2017)
- EU/other countries lining up for Free Trade deals?

The Trump administration has joined a group of countries objecting to a deal between the UK and EU to divide valuable agricultural import quotas, in a sign of how the US and others plan to use Brexit to force the UK to further open its sensitive market for farm products.

# Some current major issues (cont.)

- Political instability & uncertainty in the UK
  - Government has no overall majority in Parliament & major internal tensions
  - Population divided over what is ‘best’
  - Need for firms to know what is happening to avoid under-investment, company flight

German companies operating in the UK should make provisions for a “very hard Brexit” because the British government lacks a clear strategy on leaving the EU, Germany’s largest business lobby has said. FT, October 5<sup>th</sup>

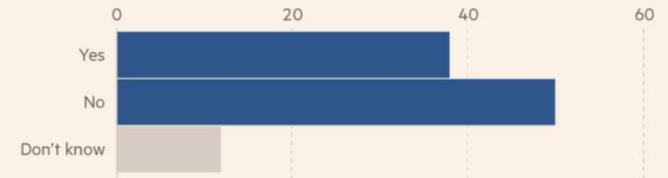
## UK manufacturing firms' building investment intentions at weakest level since 2009, finds CBI

The Independent, Oct. 23<sup>rd</sup>

The data comes amid warnings of a major fall in investment if the Government does not agree soon on a Brexit transition deal with the EU

Are you confident that the UK government will secure a good Brexit deal?

% of respondents



Polling conducted on Jun 28-30 2017

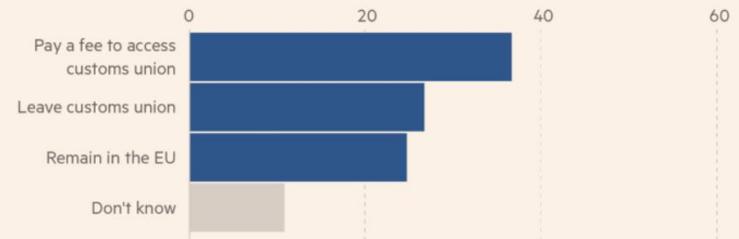
Would leaving the EU without a deal be a good or bad outcome?



Polling conducted on Jun 30 2017

Should the UK leave or stay in the EU customs union?

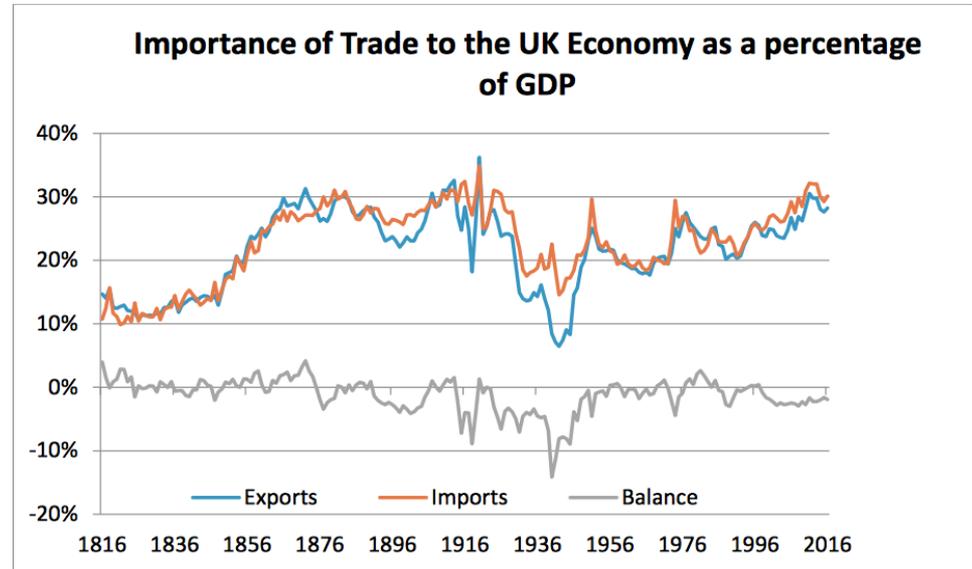
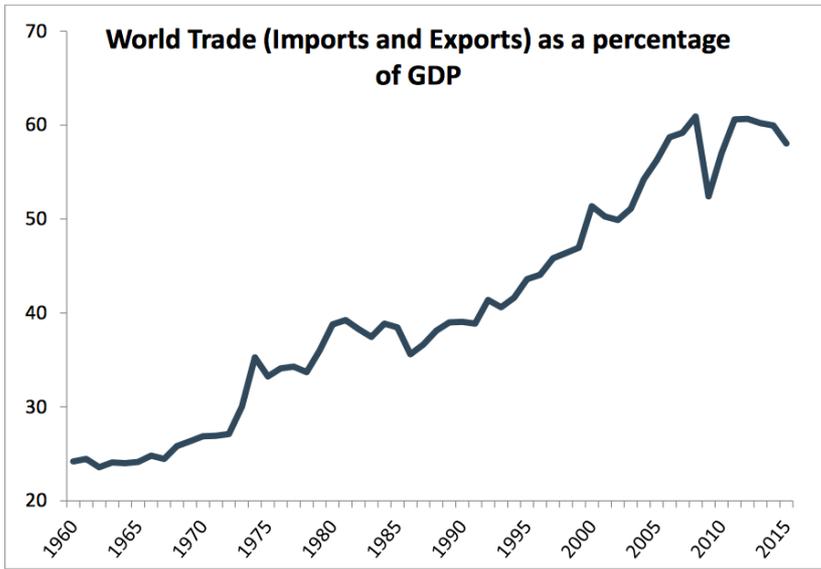
% of respondents



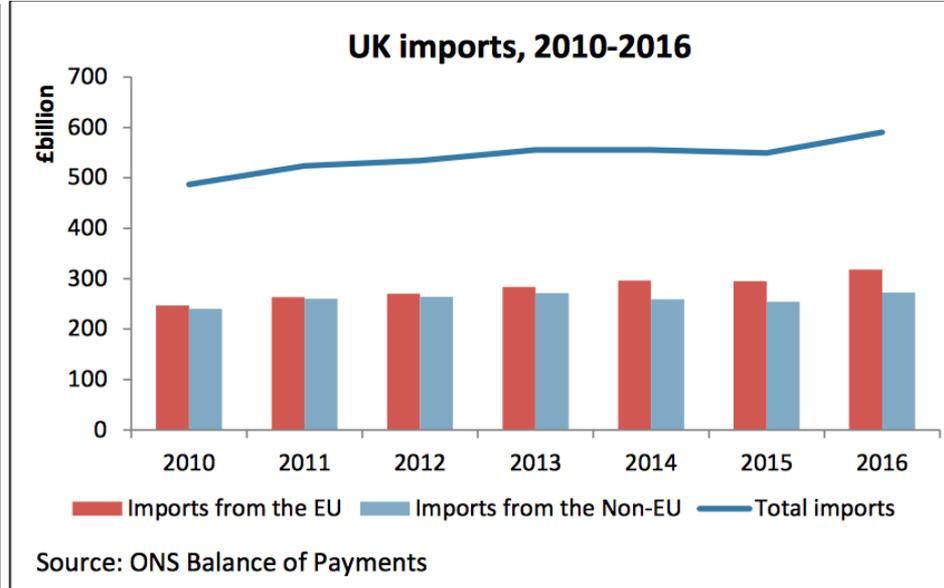
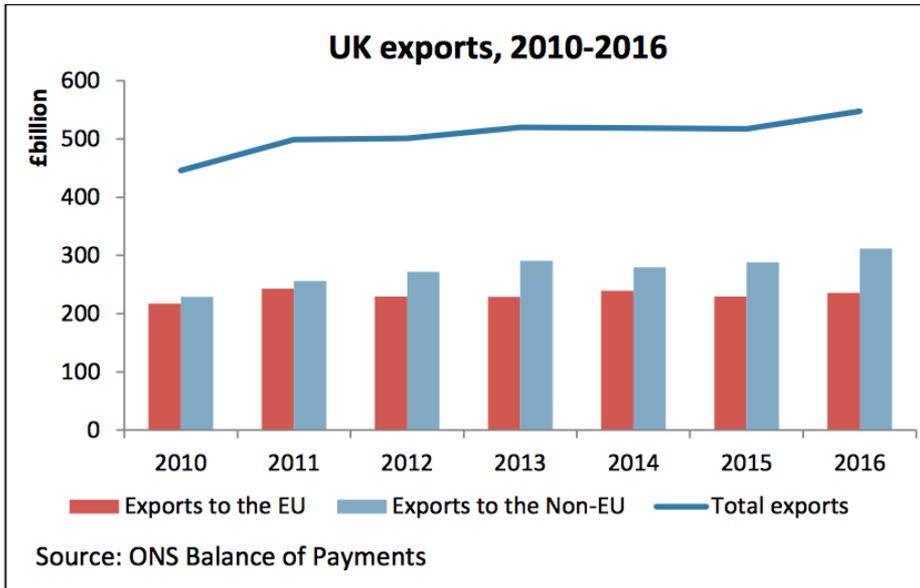
Polling conducted on Jun 30 2017

Source: NatCen Social Research © FT

# Importance of trade with EU



- Between 2010 and 2016,
  - the value of UK goods exports has grown by 12%,
  - the value of UK services exports by 40%,
  - services accounting for around 45% of the value of UK exports in 2016.
  - Trade in services represents around 20% of the value of world trade.
  - According to the OECD, services make up over 30% of the value of manufacturing exports
- Over 70% of global trade is now in intermediate products, or in capital goods



- the European Commission’s own “Trade for All Strategy” suggests, 90% of global economic growth in the next two decades will come from outside the EU, so it is likely that a greater proportion of UK trade will continue to be with non-EU countries
- All of this suggests that with respect to Brexit:
  - Trade is crucial to the prosperity and growth of the UK economy
  - Trade in services is especially important
    - Nearly 5,500 UK-based companies have passporting rights
  - Given projected growth in trade in the RoW, there are opportunities for the UK
    - But also need to take account of ‘supply-chain’ issues (next)

# Broader picture: sales/purchases

(millions of US\$)

	total intermediate EU27	total intermediates ROW	total intermediates UK	total final demand EU27	total final demand ROW	total final demand UK	Total output
Total EU27	13,912,174	1,657,519	263,366	14,025,399	1,267,817	184,599	31,310,873
Total ROW	1,463,800	65,556,448	179,246	659,972	56,400,502	142,892	124,402,861
Total UK	221,378	261,642	2,034,399	101,627	166,953	2,497,465	5,283,464
Total intermediate/final consumption	15,597,352	67,475,609	2,477,010	14,786,998	57,835,272	2,824,956	160,997,198

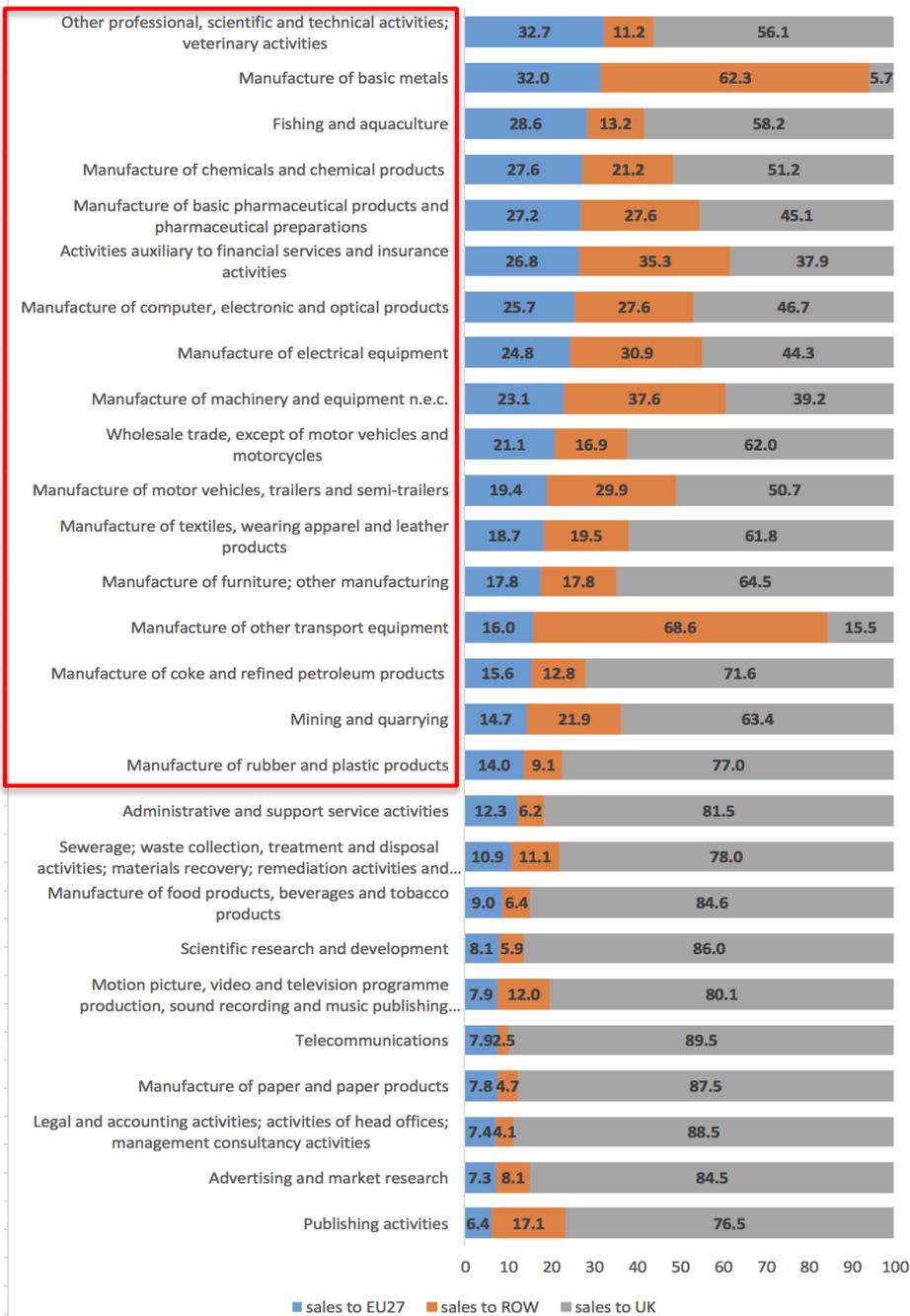
## Where sales originate:

row %	total intermediate EU27	total intermediates ROW	total intermediates UK	total final demand EU27	total final demand ROW	total final demand UK	Total output
Total EU27	44.4	5.3	0.8	44.8	4.0	0.6	100
Total ROW	1.2	52.7	0.1	0.5	45.3	0.1	100
Total UK	4.2	5.0	38.5	1.9	3.2	47.3	100
Total intermediate/final consumption	9.7	41.9	1.5	9.2	35.9	1.8	100

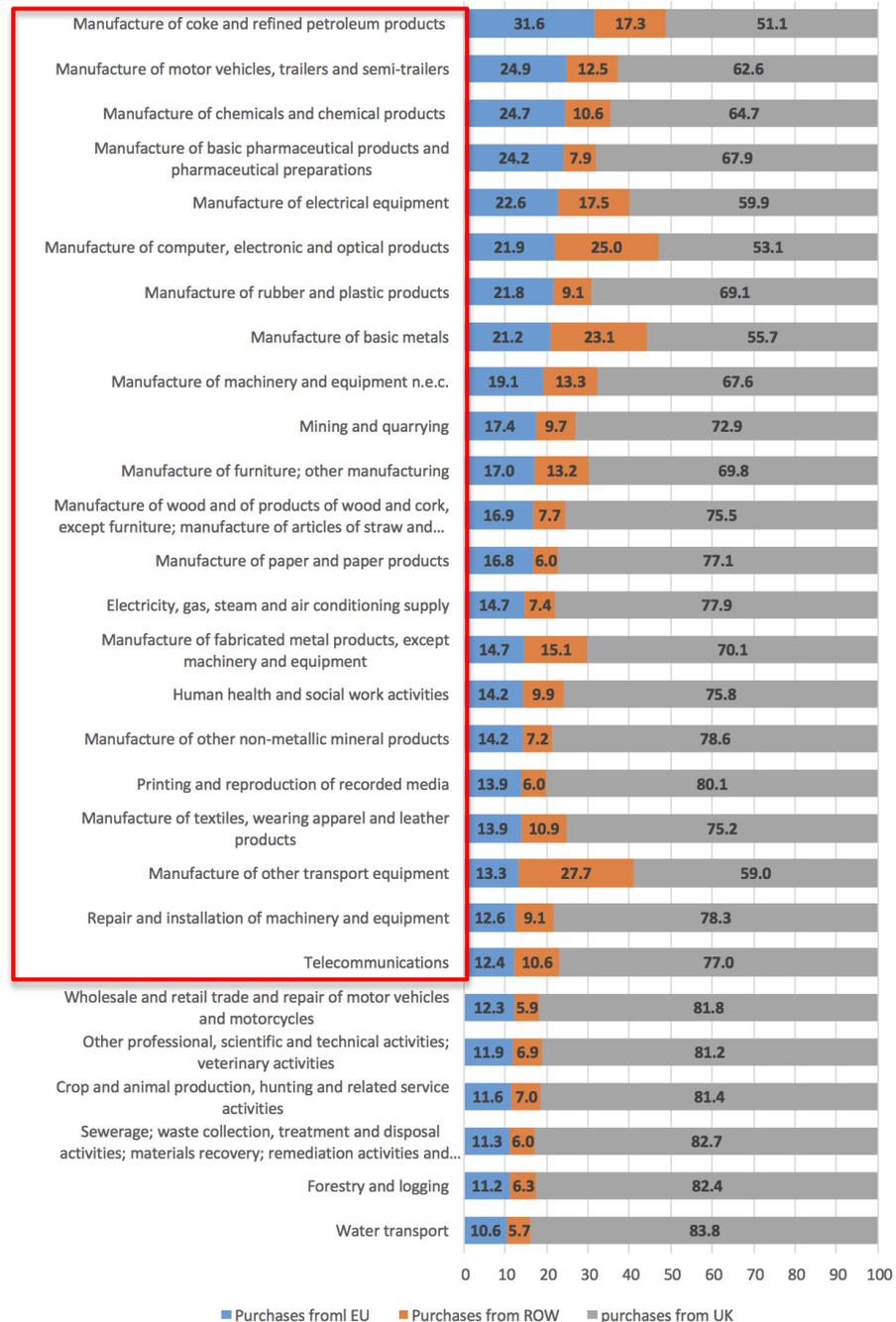
## Where purchases originate:

column %	total intermediate EU27	total intermediates ROW	total intermediates UK
Total EU27	89.2	2.5	10.6
Total ROW	9.4	97.2	7.2
Total UK	1.4	0.4	82.1
Total intermediate/final consumption	100	100	100

% of sales in 2014 to EU, RoW and UK



% of intermediate purchases in 2014 from EU, RoW and UK

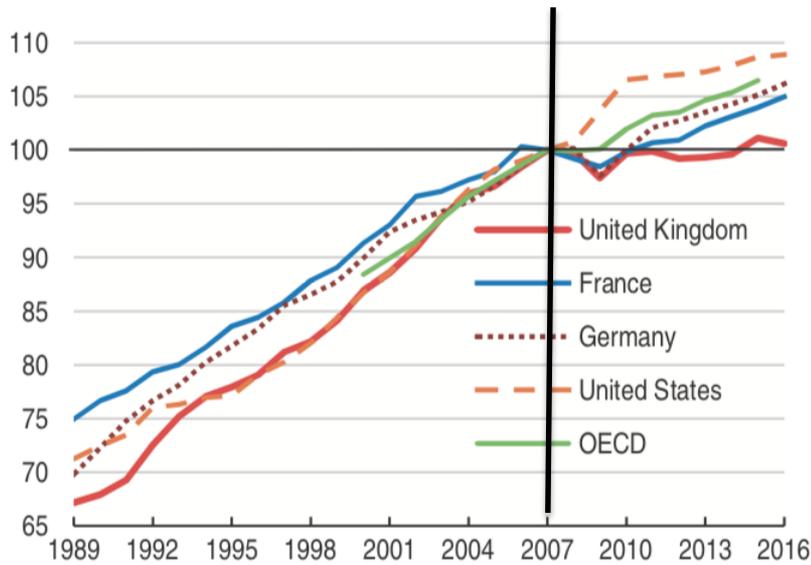


# Post-Brexit future for the UK:

Is UK well-placed to benefit from desired FT position?

- Argued by pro-Brexit economists that UK – free of EU constraint – can negotiate growth-enhancing FTA with non-EU countries
- But ‘structural’ issues that may raise doubts:
  - UK’s productivity
  - Export competitiveness and thus performance
  - Loss of EU-migrants (dealt with earlier)
  - Need to remain ‘compliant’ with EU to obtain/maintain FTA/Customs flexibility

### A. Labour productivity



### Export performance and the exchange rate



Note: Export performance is the ratio of export volumes to export markets for total goods and services.

Source: OECD Economic Outlook: Statistics and Projections Database.

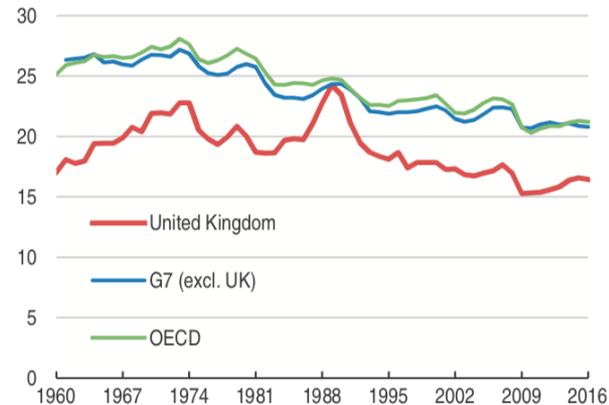
### A. Decomposition of labour productivity growth

Contributions to labour productivity growth, percentage points<sup>1</sup>



### B. Investment ratio

As a percentage of GDP<sup>2</sup>



1. Labour productivity is defined as real GVA per total hours worked. Contributions to growth are calculated using a weight of 0.67 for total hours worked and 0.33 for productive capital; total factor productivity is calculated as a residual. Productive capital excludes investment in housing.
2. In nominal terms. Investment refers to gross fixed capital formation. The aggregate for G7 (excluding the United Kingdom) (i.e. Canada, France, Germany, Italy, Japan and the United States) is calculated as an unweighted average.

Source: OECD report on UK, 2017

# Post-Brexit future for the UK: 'hard' or 'soft' Brexit?

No deal would be a “very, very bad outcome for Britain”, Chancellor of Exchequer

- OECD set-out following risks for UK

Table 2. **Medium-term shocks to the UK's economic growth prospects**

Risk	Possible outcome
Disorderly Brexit.	A break-up of EU-UK negotiations, cancelling out the prospect of a trading relationship in the foreseeable future, would trigger an adverse reaction of financial markets, pushing the exchange rate to new lows and leading to sovereign rating downgrades. Business investment would seize up, and heightened price pressures would choke off private consumption. The current account deficit could be harder to finance, although its size would likely be reduced.
Disruption of territorial integrity.	Scotland and Northern Ireland voted to remain in the European Union. Scotland could vote for independence in another referendum and the introduction of a hard border in Northern Ireland could threaten the peace process. Changes to UK's borders would have major negative economic impacts, hampering business and consumer confidence.
Political instability.	The latest general election has led to a hung Parliament, which increases policy uncertainty and reduces ability to adopt structural reforms.
Continuation of EU membership.	In case Brexit gets reversed by political decision (change of majority, new referendum, etc.), the positive impact on growth would be significant.

Table 1: Imposed tariffs and NTBs in both scenarios of Brexit.

	Soft Brexit	Hard Brexit
Tariff	0%	MFN tariff $\cong$ 4.4% in 2015 (higher on food products)
Non-tariff barrier	2.77%	8.31%

Note: The scenarios are based on [Dhingra et al. \(2017\)](#).

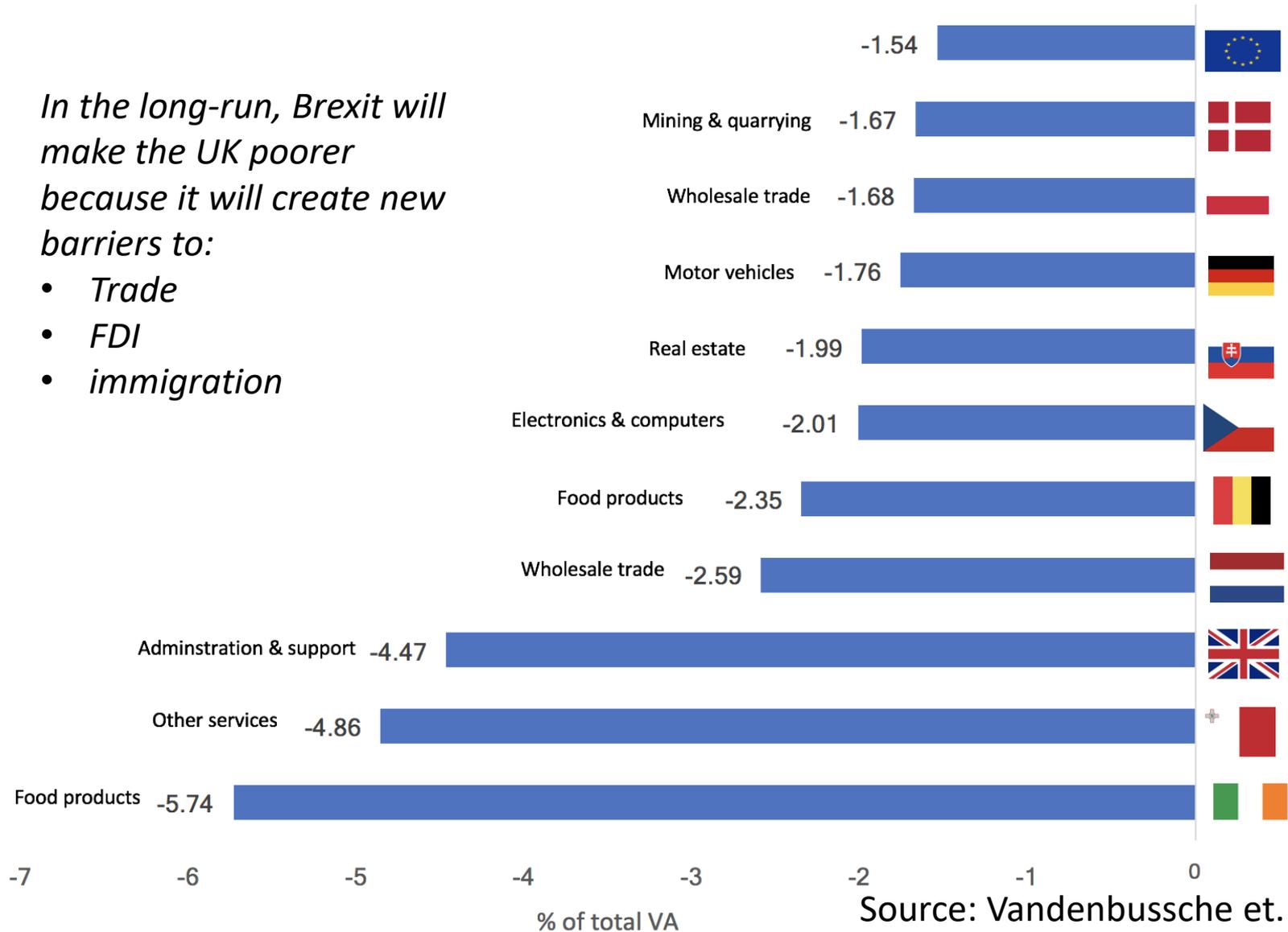
# Results from 2 recent simulations:

1.

Total long-run loss as % of VA from hard Brexit

*In the long-run, Brexit will make the UK poorer because it will create new barriers to:*

- Trade
- FDI
- immigration



Source: Vandenbussche et. al. 2017

2.

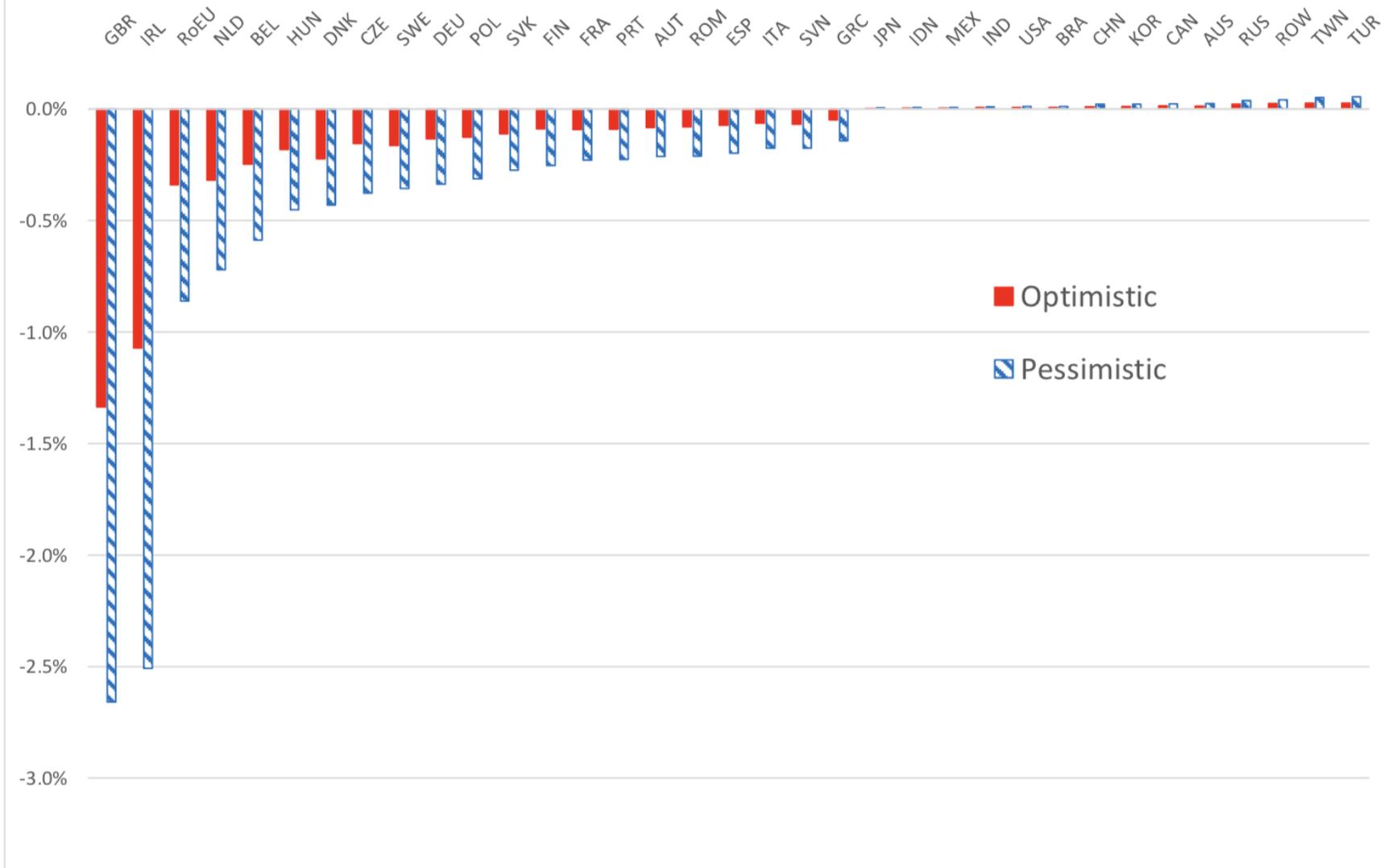


Figure 2: Estimated Welfare Effects of Brexit

Source: Dhingra et al. (2017).

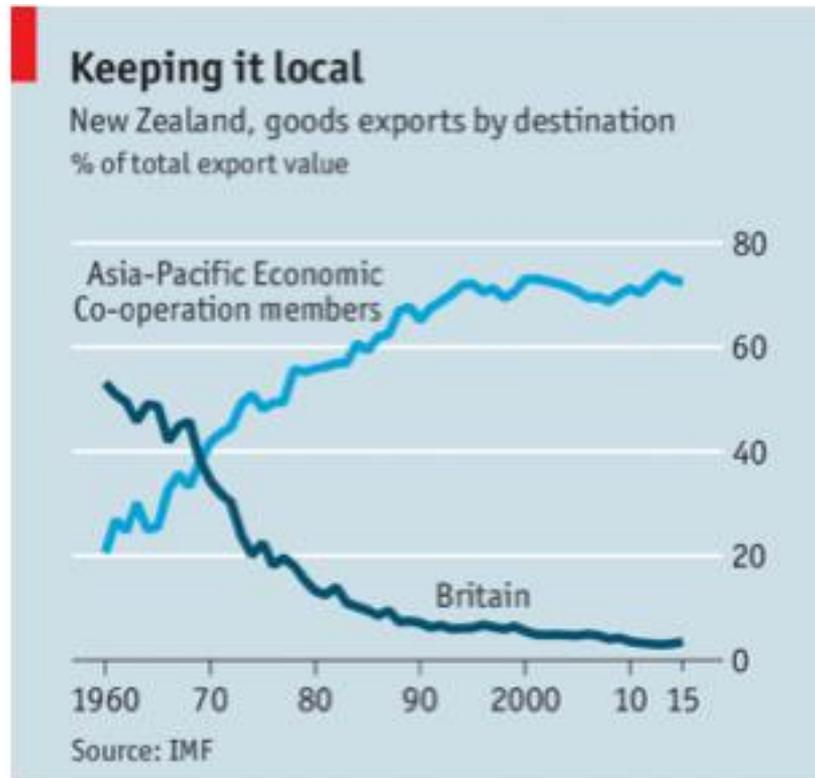
Notes: Estimates give the permanent percentage change in income per capita that has the same welfare effect as Brexit. In the optimistic scenario the UK remains in the Single Market following Brexit. In the pessimistic scenario UK-EU trade is conducted under WTO terms. See Dhingra et al. (2017) for details.

# Post-Brexit future for New Zealand

## UK will attempt to agree post-Brexit trade deal with New Zealand, Theresa May says

January 2017

Leaders of both countries highlight historic ties and shared values



# How important is UK to NZ?

OEC

COUNTRIES PRODUCTS VISUALIZATIONS RANKINGS PUBLICATIONS ABOUT API

## Destinations

The top export destinations of New Zealand are China (\$6.59B), Australia (\$5.78B), the United States (\$3.7B), Japan (\$2.08B) and South Korea (\$1.04B).

[Explore on Visualizations page](#)

[Data Sources](#)

<http://atlas.media.mit.edu/>

TOTAL: \$32.5B



DEPTH    COLOR

## Origins

The top import origins of New Zealand are Australia (\$6.38B), China (\$4.76B), the United States (\$3.57B), Japan (\$2.19B) and Singapore (\$1.46B).

[Explore on Visualizations page](#)

[Data Sources](#)

<http://atlas.media.mit.edu/>

TOTAL: \$35.7B



# Thank you

