

# Brexit – how's it going so far?

Julian Jessop

 @julianHjessop

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# 1. Agenda

- What Brexit is about
- Importance of uncertainty
- Economic costs and benefits
- Case studies
- New opportunities
- Q&A

## 2. It's not just about the economics...

"I've never met anyone who's said...

*I'd be in favour of Brexit if I thought the impact on GDP would be less than 2%, but I'll be in favour of Remain if I thought it was more than 5%*

It's the issues of identity and culture and politics that are motivating people."

Mervyn King, 2019  
(Former Bank of England Governor)



### 3. The EU's two main economic pillars

- Single Market
  - four freedoms of movement (goods, services, capital, people)
  - regulations that apply to whole economy
- Customs Union
  - no internal 'tariffs' (taxes on imports)
  - common external tariffs
  - little scope for independent trade policy



## 4. Brexit means 'taking back control' of...

1. 'Borders': end free movement of people from the EU
2. 'Laws': leave the EU's Single Market and end jurisdiction of European courts
3. 'Money': stop paying into the EU budget



And we should probably add...

4. 'Trade policy': leave the EU's Customs Union
5. 'Fish'

## 5. The costs of Brexit uncertainty

- Even before Brexit itself, the 2016 vote to leave the EU had some significant impacts on the UK economy:
  1. The value of the **pound** fell, making imports more expensive and leading to an increase in inflation (only partly offset by a boost to exports)
  2. Business **investment** stalled
  3. Some business was lost from the **City**
  4. Net **migration** from the EU slowed (only partly offset by an increase from the rest of the world)

## 6. Brexit and business investment

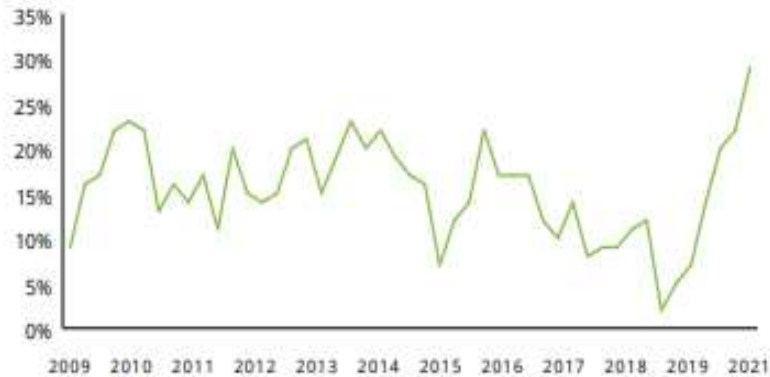


Source: Office for National Statistics

## 7. Deloitte CFO Survey (2021 Q3)

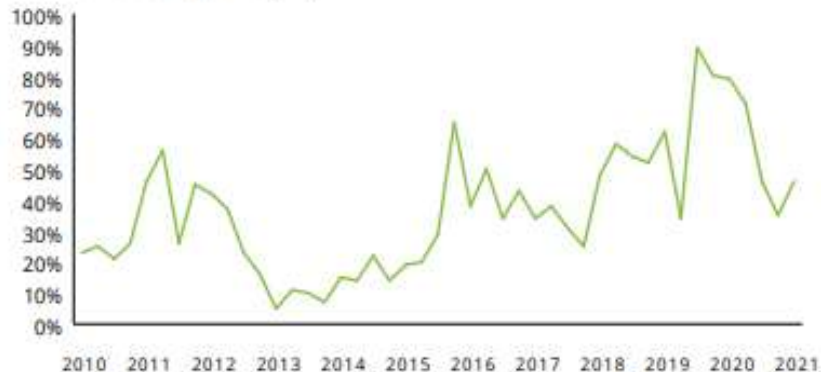
**Chart 1. Capital expenditure**

% of CFOs who rate increasing capital expenditure as a strong priority for their business in the next 12 months



**Chart 9. Uncertainty**

% of CFOs who rate the level of external financial and economic uncertainty facing their business as high or very high

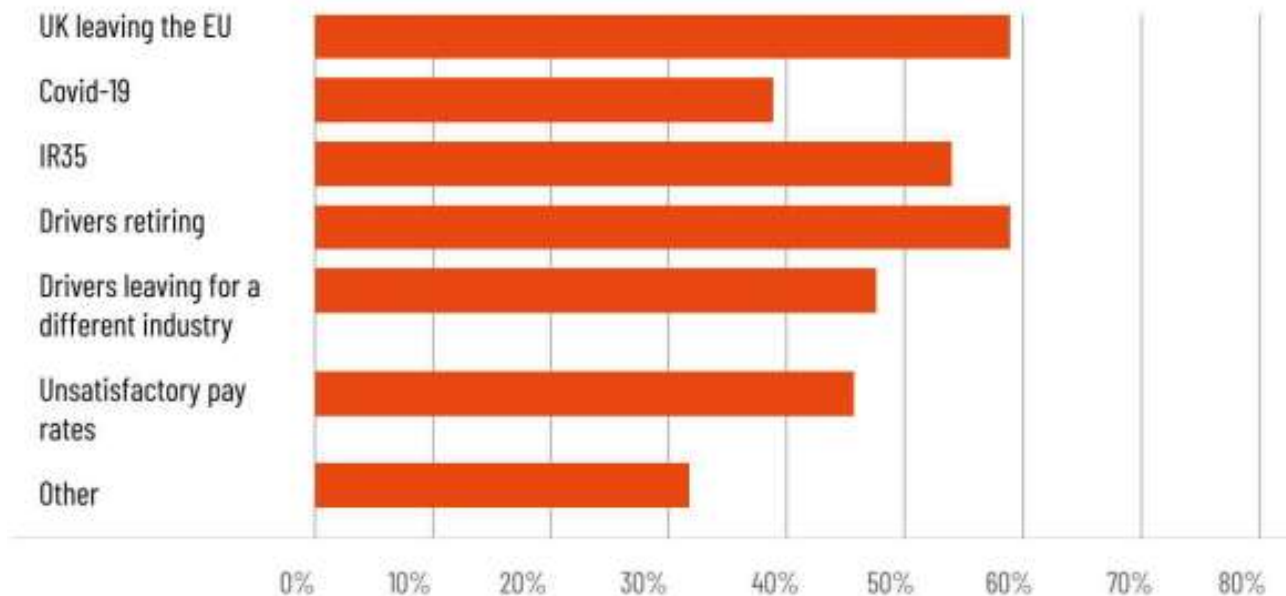


- Businesses are now planning to invest again
- There are lots of drivers here, including tax changes and labour shortages
- But the reduction in Brexit uncertainty is helping too: even businesses which are adversely affected at least now know what they are dealing with



## 8. Brexit and driver shortages

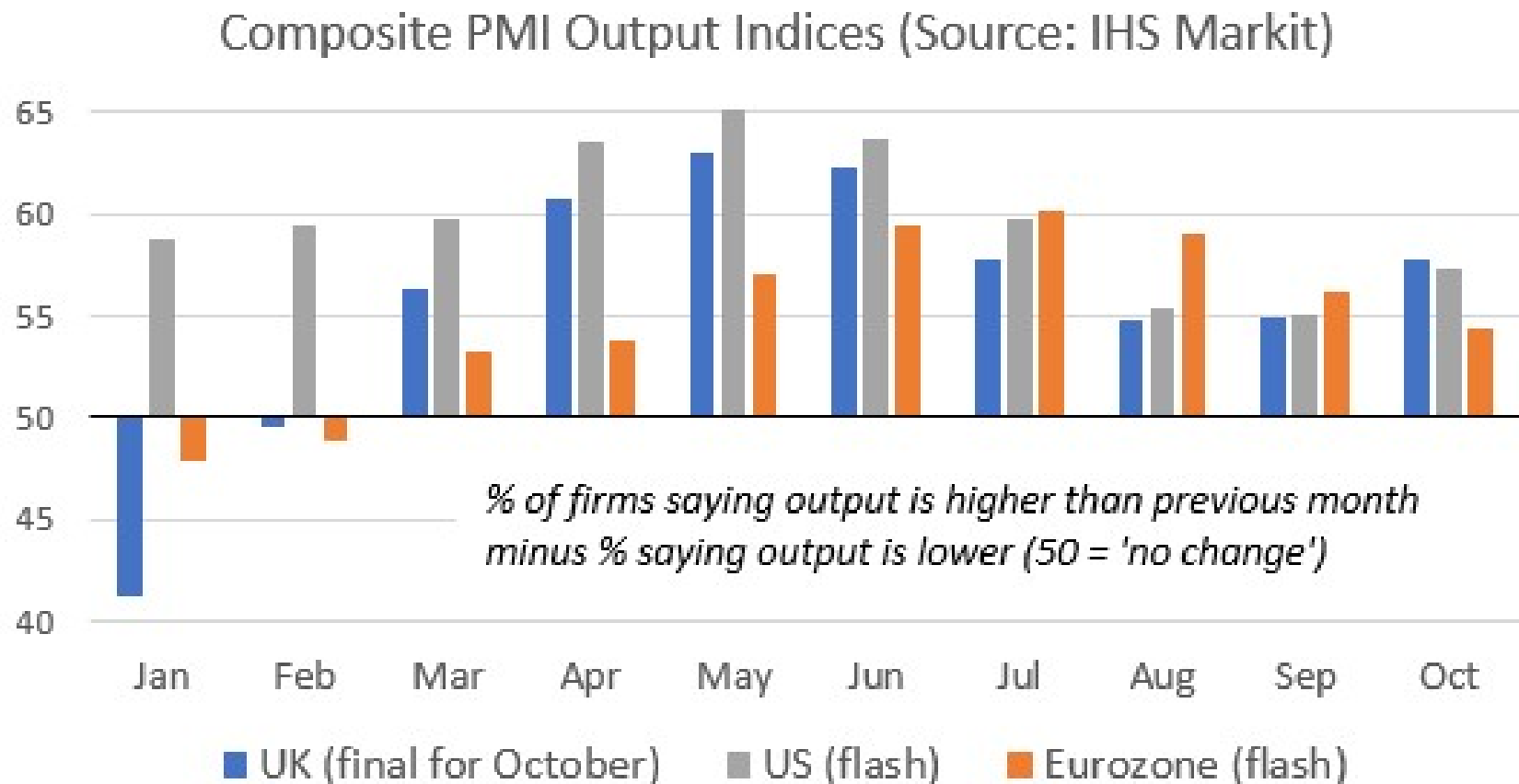
What do you believe to be the reasons behind the driver shortage?  
(please select all applicable)



## 9. Will lower immigration boost wages?

- The government hopes that reducing immigration will end the low-pay economy. That might work, in some sectors, but...
- There is very little evidence that immigration has had a significant impact on the wages of UK workers.
- See Portes (2018), “The economic impacts of immigration to the UK” (on the voxeu.org website)
- Ultimately, higher **real** wages require higher **productivity**. How does restricting the supply of labour help here?

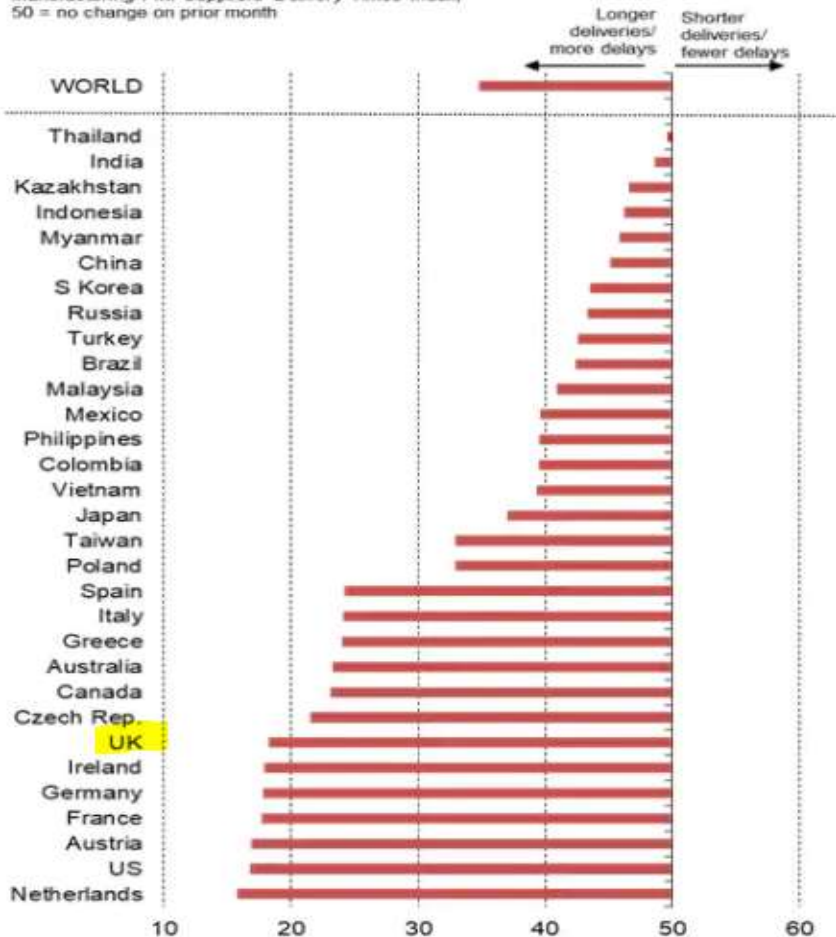
## 10. Brexit and overall economic activity



# 11. Brexit and the shortage problem

## PMI supplier delivery times index, October 2021

Manufacturing PMI Suppliers' Delivery Times Index,  
50 = no change on prior month

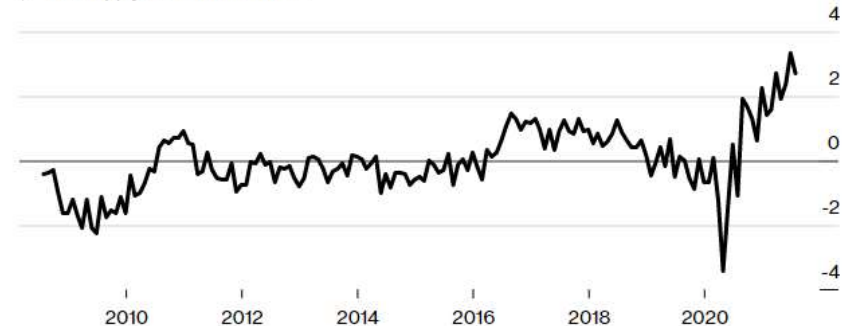


Sources: IHS Markit, JPMorgan, CBA, ISO, CIPS, au Jibun Bank, NEVI, BME, Bank Austria, AIB, AERCE, Casin, HPI, Istanbul Chamber of Industry, Tengis Partners.

## Omni-shortage

U.K. supply gauge shows shortages at a decade high

U.K. supply constraint indicator



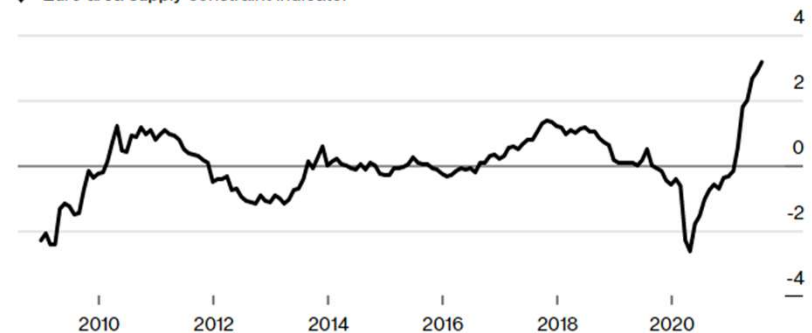
Source: Bloomberg Economics

Note: Positive numbers indicate supply deficit and negative numbers mean supply surplus.

## No Slack

Europe has shifted rapidly from excess supply to significant shortage

Euro area supply constraint indicator

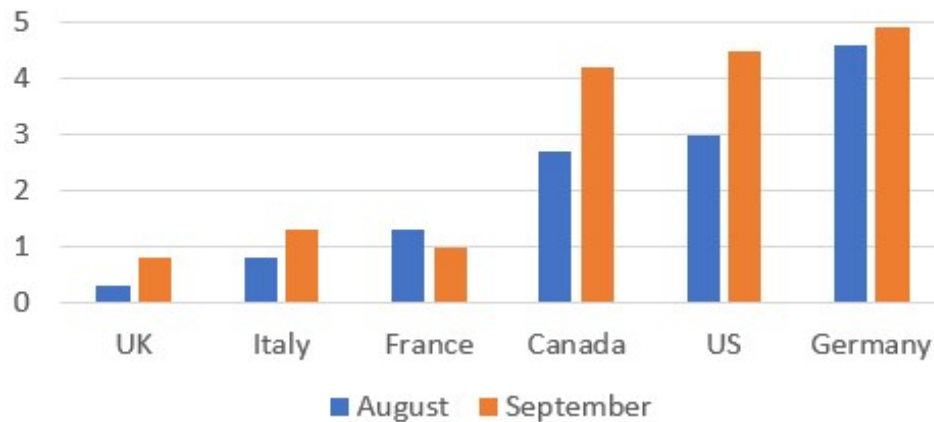


Source: Bloomberg Economics

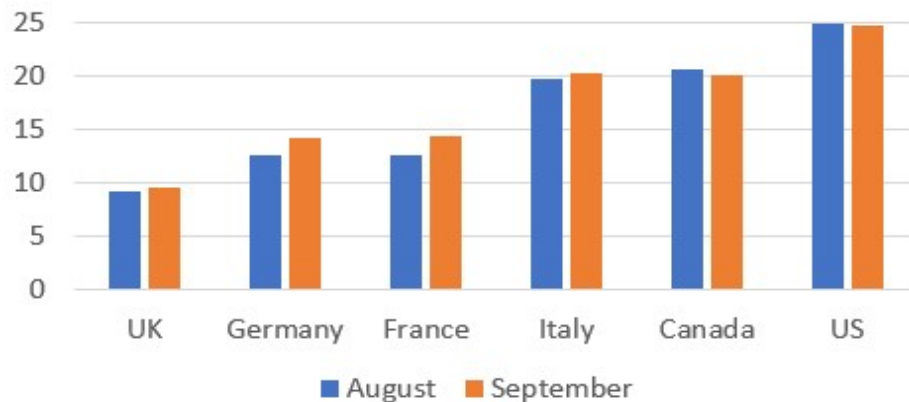
Note: Positive numbers indicate supply deficit and negative numbers mean supply surplus.

## 12. Brexit and inflation

Annual CPI Inflation: Food (%)  
(Source: National Statistics Offices)

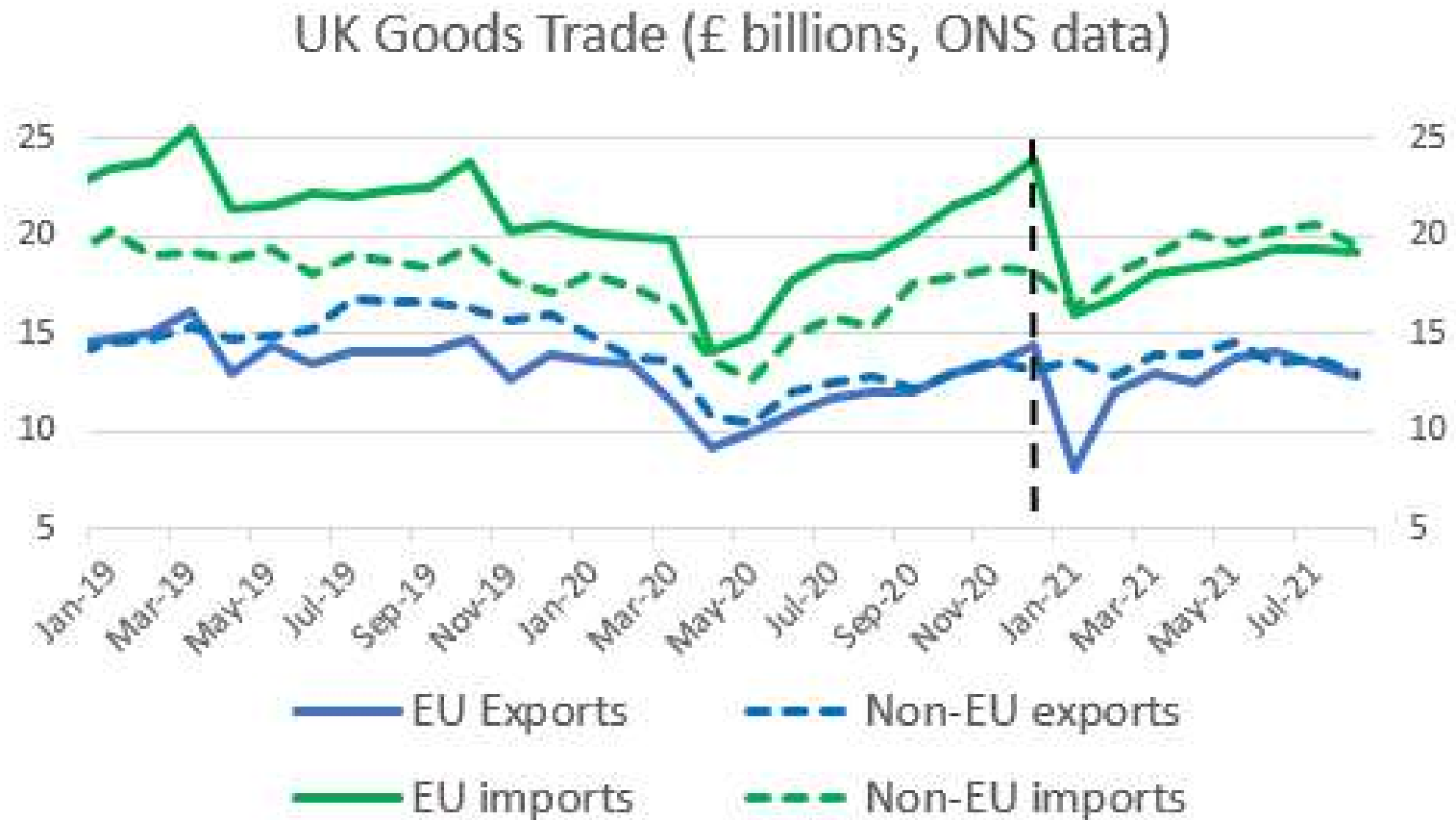


Annual CPI Inflation: Energy (%)  
(Source: National Statistics Offices)



- UK inflation has picked up and will rise further (especially in October when the energy price cap was lifted)
- But this is **global**
- Overall inflation in 'Brexit Britain' – and inflation in both food and energy prices – is still relatively low

## 13. Brexit and trade



Source: Office for National Statistics

## 14. Brexit long-term economic costs and benefits

- Potential costs
  - new tariffs and non-tariff barriers for **trade** with EU
  - knock-on effects on investment and **productivity**
- Potential benefits
  - lower barriers to trade with **rest of world**
  - freedom to determine own **regulations** and **taxes**
  - savings on contributions to EU budget
- Could go either way
  - greater control of **immigration**

## 15. Why free trade is a good thing

- Allows people, businesses and countries to **specialise** in what they do best, compared to the alternatives available to them (**'comparative advantage'**)
- Consumers benefit from **lower prices** and more **choice**
- Forces domestic producers to become more efficient
- Sharing of **skills** and knowledge
- Costs tend to be concentrated among small and vocal groups of producers, benefits are spread more thinly...
- ...but since trade is a net gain, it should be possible to compensate the losers and still be better off



## 16. The OBR view

Since our first post-EU referendum *EFO* in November 2016, our forecasts have assumed that total UK imports and exports will eventually both be 15 per cent lower than had we stayed in the EU. This reduction in trade intensity drives the 4 per cent reduction in long-run potential productivity we assume will eventually result from our departure from the EU.

- These are old **assumptions** based on work by others, rather than new analysis by the OBR
- The 4% depends both on the long-run impact of Brexit on total **trade** and (just as importantly) the knock-on effects of this on **productivity**; both are still uncertain
- The early evidence on trade is at least consistent with the OBR's view, but we have little on productivity, and it's far too soon to draw firm conclusions anyway

## 17. Case Study: Financial Services

- UK financial services firms have lost ‘**passporting rights**’ which allowed them to do business anywhere in the EU without requiring the approval of national regulators
- The EU has refused to grant ‘**equivalence**’, which would recognise the obvious truth that UK regulations are just as good as those in the EU
- Some UK firms have responded by shifting **assets** to the EU. But the number of **jobs** (and **revenues**) that have moved has been much smaller than feared
- This reflects the competitive strengths of the UK in this sector, which are largely Brexit-proof. Firms have done the bare minimum to get round the non-tariff barriers.

## 18. Case Study: Fish

- Fishing communities are far more important politically than their contribution to the economy would suggest.
- The UK fishing industry was supposed to be a major winner from Brexit, mainly because UK boats would be allowed to catch more of the fish **in UK waters**
- However, it is now much harder for UK boats to sell fish (especially shellfish) **into the EU**, which is a major market
- The EU is playing hardball, enforcing rules around issues like health and safety very strictly. The UK (the French claim) has been slow to grant licences.
- This is hurting both sides (like any restriction on trade). But that also suggests both sides will back down.

## 19. Case Study: Percy Pigs

- ‘Percy Pig’ sweets are made in Germany. The UK-EU trade deal allows them to be imported into Britain without any **tariffs**.
- The problem comes if they are then re-exported to Ireland. This means the supplier has to prove where they came from (**‘rules of origin’**) in order to avoid tariffs.
- In most cases this is easy (Percy Pigs are now flowing again). But this still requires some extra paperwork (a **non-tariff barrier**), and sometimes it is a lot harder.



## 20. Case Study: UK-Australia trade deal

- Australia farmers want **tariff-free** access to UK markets.
- UK farmers are worried they won't be able to compete. But why not?
- Lower **quality**? *Reflected in price, let consumers decide*
- Unacceptable **farming practices**? *Ban would be more appropriate*
- More **efficient**? *That's a good thing!*
- Environmental impact? *Overall carbon footprint of imports often lower*



## 21. Some Brexit opportunities

- Import **substitution** (though free trade still better)
- New **trade deals** with rest of world (EU very slow)
- Lower trade barriers **unilaterally**
- Better regulation (e.g. accounting rules, data protection, animal welfare, biosciences...)
- Drop the **precautionary approach** which is holding back innovation (the faster approval of Covid vaccines in the UK is a good example of this)
- Better **taxation** (e.g. avoiding future EU drive towards tax harmonisation, financial transactions taxes etc)

## 22. Three good sources for Brexit analysis

UK IN A  
CHANGING  
EUROPE

[www.ukandeu.ac.uk](http://www.ukandeu.ac.uk)

INSTITUTE  
FOR  
GOVERNMENT

[www.instituteforgovernment.org.uk](http://www.instituteforgovernment.org.uk)

BRIEFINGS FOR  
 **BRITAIN**

[www.briefingsforbritain.co.uk](http://www.briefingsforbritain.co.uk)

[www.julianhjessop.com](http://www.julianhjessop.com)



## 23. My conclusions

- Initial economic impact of Brexit has been negative: costs always likely to be more immediate and visible than the benefits, which will take time
- The short-term hit (especially on prices, supply chains and labour supply) is usually exaggerated, and there is still plenty of room for debate about the longer-term impacts on trade and productivity
- In the meantime, much of the **uncertainty** that has held back investment (and trade) is now clearing
- But jury is still out on how committed this government is to free trade and open markets