**RWS13 (MACRO): TRADE AND PROTECTIONISM**

**Post BREXIT: What Options does the UK face in March 2019**

***From the Financial Times – June 2017***

Just a few weeks ago, Britain’s road to Brexit seemed relatively clear. Britain’s Conservative government had made its choice, with Theresa May, prime minister, announcing that the country would leave both the EU single market and the customs union, to end the jurisdiction of the European Court of Justice and give the UK scope to strike trade deals of its own. But an election designed to bolster Mrs May’s mandate for Brexit proved a political disaster, destroying her authority and majority. Fundamental elements of her exit plan have come under increasing question.

Here the Financial Times outlines the paths available to the UK. It looks at six scenarios, ranging from a highly disruptive exit without agreement to a smoother path that sacrifices control in order to remain enmeshed in the EU’s single market. Each confronts the UK with a choice between political independence, economic performance, and the speed of change.

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| **1. NO DEAL**  The default scenario if there is no divorce agreement. The UK would no longer be bound by the EU treaties and there would be nothing to replace the thousands of international agreements that stem from them.  *Winners*  This could be hailed by purists as a “clean” Brexit. A fully sovereign Britain would be able to strike agreements with anyone unencumbered by its complex and evolving relationship with the EU. From this position, Britain could negotiate new relationships with the EU and other countries based on mutual advantage.  *Losers*  Disruption on a scale rarely seen in peacetime affecting almost every business in Britain. The lack of customs facilitation deals would disrupt trade at borders, air traffic would be hit by a lack of regulatory approval to fly to the EU, British lorry drivers would not be licensed to drive their vehicles in the EU. The transportation of nuclear material to Britain would cease. Tariffs on goods would be imposed at tight border controls. Food imports would be a problem.  A hard border in Ireland would spring up overnight. Any areas in which the UK had not legislated for a replacement regulatory agency would be left hanging. The residence of EU citizens in the UK and British citizens in the EU would be left to the mercy of their host country governments. The EU would also lose out because of the disruption to trade and the hole in the bloc’s current budget that would be opened up by a failure to reach a deal.  *Timing*  Could take place in March 2019, as soon as the UK leaves the EU.  *FT verdict*  Philip Hammond, the UK chancellor of the exchequer, says no deal would be a “very, very bad outcome for Britain”. It is worse than that. It is simply not a viable option. There are almost no winners and the UK would be pursued in international courts for money the EU claims it owes. The government’s “no deal is better than a bad deal” bravado has receded; most officials concede this would be a self-inflicted wound of historic proportions. | **2. DIVORCE-ONLY AGREEMENT**  Less disruptive than a no deal scenario. The UK would strike an Article 50 agreement with the EU on its departure from the bloc, but would leave the future relationship to be negotiated from the outside, with interim trade based on World Trade Organization rules. This is still a very hard Brexit, since there is no agreement to replace EU membership, but the two sides would have come to a mutual understanding rather than a position of conflict.  *Winners*  By hugely increasing trade barriers with the EU, Britain would need to become more self-sufficient. Winners would include domestic suppliers to UK manufacturers who would not face as much competition.  In the longer term, companies oriented towards trade with countries with which the EU has no preferential deal might gain if the UK could strike a worthwhile free-trade deal more quickly. UK companies would have greater scope to lobby for state aid and contracts from the British government, currently outlawed by single market rules.  *Losers*  Companies involved in EU-British trade on both sides of the channel would be hit by tariff and non-tariff barriers as well as the ability of governments to discriminate against them. Tariffs would be up to 10 per cent in the automotive sector, about 22 per cent on agricultural products and up to 59 per cent on specific items such as beef. Customs delays would still be significant at the hard border and behind it as companies would need to fill out rules of origin declarations.  *Timing*  Would take effect in March 2019.  *FT verdict*  Could prove to be one of the most protectionist steps in UK peacetime history. The increase in trade barriers with the UK’s biggest market would make the nation more insular with no guarantee that alternative trade deals would supplant the EU. The freedom to set the UK’s rules would encourage Britain to become an offshore tax haven, such as Bermuda. Meanwhile, it would abruptly lose all its current preferential trade terms with non-EU countries, since they were negotiated by the bloc. | **3. LIMITED TARIFF-FREE DEAL**  Britain strikes a limited free-trade agreement with the EU to maintain tariff-free trade in goods. The UK is free to agree deals with other countries, but there would be no guaranteed access to the EU market for the services sector. Customs checks would still add friction to trade with the EU and companies could have to duplicate their production lines, making some goods that satisfied UK regulations and others that met EU rules where these differed with Britain.  *Winners*  Since Britain ran a £95bn goods trade deficit with the EU in 2016, the main winners would be EU manufacturers who could sell to the UK without facing tariffs — the likes of Fiat, BMW and Siemens.  UK manufacturers, particularly in the automotive sector, would also stand to gain compared with trading on WTO rules. Industries such as pharmaceuticals and aerospace would benefit from a tariff-free deal instead of relying on WTO rules.  *Losers*  The service sector would be excluded from a limited tariff-free deal on goods. Britain had a £88bn trade surplus in services, which account for almost 80 per cent of the UK economy. Financial services would lose “passports”, which confer the right to sell banking, insurance and other financial services across the EU. Other services sectors, including gaming, architecture and professional services such as management consultancy would still be hit. Companies with complex supply chains would still have to deal with non-tariff barriers and delays at overburdened customs posts. Agriculture is also not a standard part of such trade agreements.  *Timing*  Probably only after 2019.  *FT verdict*  This is quite a likely outcome, since the EU would like a free-trade deal in goods and such a deal is much easier to agree than deals on facilitating trade in services. But it would do little to help Britain’s service sector-oriented economy and some of its high-tech manufacturing activities. It would make the UK a little like Canada in its dealings with the EU. The burden to re-establish trading relations with non-EU countries would still be enormous. |
| **4. FAR-RANGING TRADE DEAL**  Britain would sign a bold and comprehensive trade deal with the EU covering most aspects of trade with the bloc. But the more comprehensive the deal, the more limitations on sovereignty the UK would have to accept.  *Winners*  Compared with a deal only on goods, the service sector would benefit from a deeper free-trade agreement. It is rare for financial services to be covered in such an accord, but British negotiators argue that it will be easier to include the sector than is usually the case since it currently is in full compliance with EU rules. Ensuring regulations are equivalent and accepting EU regulatory oversight of financial services in London might enable some financial services to continue to sell to the EU from London. Other parts of the services sector would also benefit from more relaxed rules on movement of labour, even if these were more restrictive than current free movement rules.  *Losers*  The UK would in many areas become an EU rule taker rather than a rulemaker. Manufacturers would still have to cope with additional red tape in customs procedures. Rules ensuring a level playing field with other European companies would disappoint British groups hoping to benefit from UK public contracts and subsidies. Companies complaining about the burden of EU regulation on everything from capital requirements to environmental standards see no real change.  *Timing*  The EU side insists that a fully fledged trade deal could not be agreed while the UK is a member. It could take years to put into practice.  *FT verdict*  As is the case today, Britain would not have full freedom to set subsidies without reference to the rest of the EU. Unlike today, the UK would not have a direct say in EU law and regulations. This outcome would maintain substantial payments to Brussels and probably continued EU influence over British law. While borders and trade with the EU would not be frictionless, the disruption would be far less than in harder Brexit scenarios. The UK would also be free to look for other trade deals outside the EU. | **5. CUSTOMS UNION**  Agreeing a new customs union with the bloc would seek to smooth, as much as possible, trade at the UK-EU border. It would allow Britain to negotiate its own deals for services, and agriculture, and set many domestic regulations but external goods tariffs and goods trade deals would be run by the EU. Turkey, which has similar arrangements, shows that they do not lead to wholly frictionless trade, but many non-tariff barriers would be significantly mitigated.  *Winners*  Britain and Europe’s manufacturing sectors would be delighted by this arrangement. There would be no need for physical checks that goods were not from outside the customs union and British companies would benefit from EU trade deals currently under negotiation.  *Losers*  Goods that are sensitive and do not necessarily conform with EU regulations would still face enhanced customs checks and possible delays compared with today. Agriculture might not be included and the service sectors would not benefit from a customs union only deal. But the customs union could be appended to other forms of Brexit including a deep and special free-trade agreement which sought to maintain liberalised trade in these areas too.  *Timing*  The British government has ruled out remaining in the customs union, but has also said that current customs border arrangements will need to remain in place during an “implementation period” after 2019.  *FT verdict*  A customs-only agreement would preserve many aspects of Britain’s current trading relationship and protect manufacturing jobs. But while remaining in such an arrangement, the UK would not be able to strike tariff reduction agreements in goods trade with countries such as the US and China — one of the principal rationales for Brexit. If the EU were to agree to keep the UK in customs arrangements, it would also probably seek to avoid being undercut by obtaining assurances that British tax and regulations would remain similar to its own rules. | **6. SINGLE MARKET**  Were Britain to remain in the single market by retaining membership of the European Economic Area — either with a customs union agreement or without — it would ensure continued regulatory harmony with the EU and tariff-free trade. This would guarantee that any goods and many services placed on the market in the country could be sold in any EU state. If the agreement included customs and agriculture, it would be equivalent on the trade side to continued EU membership.  *Winners*  The City of London would continue to be able to sell financial services to the EU using passports. Large companies, food manufacturers, construction companies and other employers of EU labour would also gain as Britain would have to accept the free movement of labour as part of a deal to remain inside the EEA. Such a move would allow employers to continue as today without facing huge disruption to regulatory rules.  *Losers*  The losers would be people who wanted the UK to take back control over its affairs from Brussels. The European Court of Justice would maintain a big role in interpreting law that applies in the UK. Britain would have to accept EU regulations without much influence on them. People in trades competing with European labour would face relatively unchecked EU immigration. If Britain was outside the customs union, domestic exporters would have additional and burdensome customs forms to complete.  *Timing*  Some critics say the difficulty of fashioning a bespoke transition deal before 2019, let alone a final trade accord, means the UK will have to choose between a very hard Brexit and remaining in the single market on current terms for years to come.  *FT verdict*  This outcome would maintain most of Britain’s economic ties with the EU, particularly if combined with a customs union agreement. But the UK would not gain much control over its affairs that it does not already have. In purely economic terms, it is difficult to see advantages of this arrangement compared with membership of the EU itself, but it is the least disruptive Brexit. |