Appendix A: Summary of Assessments of Economic Impact from EU Transition

The following section sets out the latest assessment of the key areas of policy risk and evidence in terms of both the immediate period after the UK exits the EU and the medium to longer-term.

Short term risks have primarily been addressed through Business Continuity Plans and the work of the Local Resilience Forum, whilst medium to longer term risks will be actively monitored together with our partners and the Forum, and any wider impact on the Council will be addressed in our future organisational planning including our Medium Term Financial Strategy and Commissioning.

State of the economy – December 2020

Overall, it will be difficult to isolate the effect of the end of the transition period from the ongoing effects of the pandemic. We know that the Coronavirus pandemic has shocked the economy in a way which has supressed GDP and could lead to increased unemployment in future.

The most recent official estimates by the Office for Budget Responsibility, released at the same time as the Spending Review in November, outlined three broad scenarios:

- Upside – the vaccine is effective and growth rebounds strongly to pre-pandemic levels by Q4 2021, and unemployment peaks at 5.5%
- Central – the vaccine is effective, but some ongoing limited lockdown is required. The economy returns to pre-pandemic growth in late 2022 and unemployment will peak at 7.5%
- Downside – the vaccine is ineffective at controlling the virus, Public Health measures continue. The economy recovers by 2024 and unemployment reaches 11%.

Both the central and downside scenarios have long-term ‘scarring’ of 3-6% of GDP reflecting the permanent damage to the economy. The OBR have assumed that in all three scenarios a Free Trade Agreement is reached with the EU. Should one not be reached, the OBR have suggested the initial impact would be about 2% reduction of GDP initially, and then 1.5% in future.

The impact of leaving the Single Market

Due to the sheer enormity of the economic impact from Coronavirus, it is not a simple task to identify a specific ‘impact’ from the end of the transition period. Since the referendum an array of suggestions about the scale of the impact have been made and these are summarised at the end of the appendix.

Part of the challenge is that leaving the single market is different from the impact of the pandemic. Although the pandemic has affected all sectors of the economy. It has done so to varying degrees, with the main impacts felt on high streets in accommodation and food sectors, construction and transportation. The severity of impact in accommodation and food reflects the reality of the lockdowns which have prevented people going out. Accordingly, as restrictions are lifted, there is a chance of these sectors having some growth, and should this continue these sectors are unlikely to be effected by the UK leaving the single market.

With the end of the transition period, those sectors which rely upon access to the EU are likely to experience the main impact. The overall effect will be contingent on nature of the trade deal agreed and the effects would not be felt evenly across different sectors.

For example, analysis by the Institute for Fiscal Studies, highlights that Manufacturing is around 9% of the UK's GVA yet around 50% of its trade is with the EU (£138bn). Comparatively, non-financial services are 60% of GVA (2017 figures), and about 51% is traded with the EU (£265bn).

What we can suggest is that the 'cost' of leaving the Single Market is based around a mixture of non-tariff barriers (a cost of doing business) and direct tariffs. The IFS suggests that these are equivalent to between 9% (FTA) and 13% (No Deal) of the value of trade.

This would mean for example new trade related costs of between £23-34bn for non-financial services. However, the exact timing of those costs, the impact of government policy and shifts in exchange rates could all contribute to mitigating those costs.

The essential point is that a shift to a different trade relationship, even with a deal, would create costs for UK based businesses.

Within Warwickshire to a certain extent the impact of our Recovery approach in response to Coronavirus will have crossover impacts around transition. The difference in effects from a new trading context for different industries will likely mean a specific set of impacts for certain key groups will become clearer over the medium term.

Essentially, although the effects of leaving the single market is highly dependent on the type of deal struck with the EU; the effect of any change in trade terms with a large market such as the EU could have a variety of effects on employment and business conditions.

Official Assessments

- HM Govt’s (November 2018) modelled scenarios suggested that:
    - A ‘no deal’ could cause between -7.7% & -9.3% reduction in GDP depending on migration impacts
    - A free-trade agreement between -4.9% & -6.7%
    - The proposed Govt. white paper -0.6% to -2.5%

- The Office for Budget Responsibility has produced two sets of reports this year:
    - In July, the Fiscal Sustainability Report had a model which indicated that GDP would fall by 12% before growing by 9% in 2021 and 4% in 2022. This projection reflected the best-known array of impacts from the Coronavirus pandemic plus the impact from a Free Trade Agreement.
    - In November, the OBR ‘central’ forecast was updated, they suggested that the economy shrank by -11.3% in 2020, and would grow by 5.5% in 2021, and 6.6% in 2022. These higher numbers reflect the recovery from unwinding of public measures in response to the pandemic.

Other Assessments

- The Bank of England: The November Monetary Policy Report contains a chapter ‘The transition to a new UK-EU trading relationship:
    - Based on the routine survey which the BoE undertakes, it has found that around 19% of its surveyed firms have no EU trade, 40% of firms are ‘as ready as they can be’ and overall around 1/3 of firms surveyed are ‘partially prepared’.
    - The expected reduction in exports, and the impact on domestic supply chains, reduces projected GDP directly by around 1% in 2021 Q1. These effects are expected to dissipate by the end of 2021 Q2 as more businesses adjust to the new arrangements.

- The Institute for Fiscal Studies in its recent ‘Green Budget 2020’ has outlined its analysis of the overall impacts of adjustment within the economy.
- Their analysis has attempted to draw together the like adjustment for firms from both the pandemic and the end of the transition period.
    - They believe that by 2024/25 economic output will be 4.5% smaller than projected by OBR March projection. 1.5% of this will be due to ‘Brexit’ and the remainder (3.2%) due to Covid-19.
    - The IFS projection is a lot higher than most official estimates and reflect the potentially larger cost of economic reconfiguration.