UNITED KINGDOM: WHAT WILL BE THE ECONOMIC CONSEQUENCES OF A HARD BREXIT?

With only a few weeks left before the end of the transition period that has extended the United Kingdom's de facto membership of the European Union, considerable uncertainty remains about Brexit and its consequences. Whatever the outcome of the current negotiations on a free trade agreement, it is clear that this will be a hard Brexit. From this observation, a number of important questions emerge. What will be the consequences of the UK's withdrawal from both the EU's single market and customs union? What effect will Brexit have on the UK economy, and will it differ across sectors? How will Brexit influence future economic policy in the UK?

Since its official withdrawal from the European Union on 31 January 2020 – made possible by the ratification of the EU-UK Withdrawal Agreement (the Withdrawal Agreement) – the United Kingdom has entered a transition period during which EU law continues to apply. In particular, during this period the country remains in the EU's single market and customs union, continues to apply EU policies in justice and internal affairs, remains subject to the EU's executive mechanisms, and has to observe all international agreements signed by the EU.

Although the Withdrawal Agreement allowed for this transition period to be prolonged by up to two years by mutual agreement, the UK has refused any extension. The transition period will therefore end, as initially planned, at the end of the year. At this point, the UK will, in accordance with its wishes, leave the EU's single market and customs union. This hard Brexit will have an impact not only on the trade relationship between the two parties, but also on the exchanges between the UK and the rest of the world. This in turn will have repercussions for the UK economy as a whole – even though its sectors will be differently affected – and thus for the country's economic policy.

The EU's single market and customs union

Also known as the common market or internal market, the single market has, since its creation in 1993, ensured the free movement of people, goods, services and capital – the "four freedoms" – within the European Union. Its primary goal is to facilitate trade and business between its members, by removing technical, legal and bureaucratic obstacles. For example, the free circulation of goods is guaranteed by the removal of customs tariffs and quotas, the principle of mutual recognition, the removal of physical and technical barriers, and the promotion of standardisation.

The twenty-seven members of the European Union, together with the UK until the end of the transition period, are full members of the single market. In addition, the single market has been partly extended to three of the four current members of the European Free Trade Association (EFTA) – Norway, Iceland and Liechtenstein – since the Agreement on the European Economic Area (EEA), which now covers these three countries and all EU member states, entered into force on 1 January 1994. This extension is only partial as it excludes certain dispositions, such as the EU's Common Agricultural Policy (CAP) and Common Fisheries Policy (CFP), resulting in the possibility, and indeed the existence, of customs tariffs on agricultural products traded between the three countries and the EU. However, this partial access to the single market comes with conditions. In return, Norway, Iceland and Liechtenstein must respect the four freedoms, contribute to the EU budget, and incorporate EU law relating to the internal market into their domestic legislation. Meanwhile, Switzerland, the fourth EFTA member, rejected EEA membership in a referendum. However, the country also enjoys partial access to the single market, thanks to more than a hundred bilateral agreements with the EU.

The EU, along with Monaco, also forms a customs union. This has three main implications: no customs tariffs are applied to goods moving between EU countries; member states apply a common tariff for goods imported from third countries; and goods that have been legally imported may circulate freely on the whole EU territory without customs checks.

At the same time, the EU belongs to three other customs unions, with Turkey, Andorra and San Marino. The union with Turkey covers only industrial and transformed agricultural goods. Such goods can therefore move freely between the two parties, that is to say without being subjected to tariffs or quotas. In addition, Turkey applies the EU's common external tariff, and it aligns with the EU acquis – that is to say with its legislation – in several areas, most notably regarding industrial standards. Lastly, while Turkey has the right to negotiate and conclude free trade agreements with third countries, it does so in parallel with the EU.

The EEA is not a customs union, as there is no coordination of customs tariffs. It is therefore possible for a country to be part of the single market without belonging to the EU's customs union. This is true of Norway, Iceland and Lichtenstein. It is also possible to be a member of the customs union without being part of the single market. This is the case for Turkey, which is therefore not required to fully respect the four freedoms.

The effects of leaving the single market and customs union

While the UK voted for Brexit in 2016, the country could have left the Union while retaining access to the single market, for instance by joining the EFTA in order to remain within the EEA. After all, the EFTA was created on the UK's initiative, and the country only left it in 1973 in order to join the EU.

However, former Prime Minister Theresa May and her successor Boris Johnson have both refused to remain in the single market. In her Lancaster House speech of 17 January 2017[1], Mrs May ruled out this possibility, as it would require continuing to respect the four freedoms, adhering to regulation over which the UK had no influence, and remaining under the jurisdiction of the European Court of Justice (ECJ). According to her, this would mean *"not leaving the EU at all"*.

After leaving the single market, the UK will become a "third country" in the eyes of the EU. The country will therefore lose a significant degree of fluidity for its exchanges with EU member states. Admittedly, a free trade agreement, as proposed by the EU, would prevent the introduction of customs tariffs or quotas for goods traded between the two parties. However, such an agreement would not prevent the emergence of numerous non-tariff barriers to trade in both goods and services. In the case of goods, these may include additional procedures, notably

1 The government's negotiating objectives for exiting the EU: PM speech, United Kingdom Government, January 2017.

to meet EU standards, and enhanced customs controls, resulting in additional costs and border delays for UK exporters. Moreover, should regulation and standards in the UK and the EU gradually diverge, such barriers could develop over time. Even if a free trade agreement is reached, traded goods will need to meet rules of origin – precise criteria to determine the origin of products – in order to be exempted from tariffs and quotas.

In addition, the UK government has refused to remain within the EU customs union, because of its willingness to negotiate free trade agreements with third countries independently. This means that the country will no longer benefit from the trade deals that the EU has struck with third countries. The UK is therefore currently negotiating with the rest of the world to replicate these agreements and find new ones. Another consequence of leaving the EU's customs union is that the UK will use its own set of tariffs for its imports, the UK Global Tariff (UKGT). It is true that more than 15% of tariffs have been cut to zero, and that some others have been reduced or simplified. However, the UK has not yet replicated all EU agreements, which means that these new tariffs will apply to a greater share of its trade. To date, the UK has reached agreements with just over fifty countries, which represent nearly 12% of its total imports and exports. By comparison, the countries which have signed trade agreements with the EU represent around 16% of total UK trade.

If the UK does not reach a free-trade agreement with the EU, these tariffs will also apply to its imports from the EU – which account for more than half of the UK's total imports. The additional costs from tariffs and non-tariff barriers will in turn certainly be passed through to prices, thus reducing the purchasing power of UK consumers. At the same time, UK exports to EU countries would be subject to the EU's Common Customs Tariff (CCT). According to the UK's largest employers' organisation, the Confederation of British Industry (CBI), UK companies will face tariffs on 90% of their exports to the EU, which would clearly damage their competitiveness.

Estimating the impact of Brexit

While there are large uncertainties, the immediate shock to the UK's economy following its effective withdrawal from the EU could be substantial. According to a survey undertaken by the Institute of Directors[2], one quarter of business leaders were unsure in September whether their company would, by the end of the year, be prepared for the end of the transition period. In a letter to logistics groups[3] dated 22 September, Michael Gove, Minister for the Cabinet Office and responsible for Brexit preparations, alerted to the risks faced by the sector at the end of the transition period. Under the "reasonable worst-case scenario" (RWCS), between 40% and 70% of UK trucks travelling to the EU "might not be ready for new border controls". In addition, a lack of capacity at border points could reduce the flow rate to between 60% and 80% of normal levels, leading to queues of up to 7,000 trucks in the UK and to delays of up to two days.

The shock could be particularly large in the scenario of an exit without a deal. A study from the UK Treasury in 2016[4] estimated that in a scenario in which the UK remained within the EEA – something that is no longer an option – GDP would be after two years 3.6% lower than it would have been if the country had remained in the EU. In the scenario of a no-deal Brexit, GDP would be 6% inferior. In November 2018, the Bank of England[5] estimated that, under an exit scenario defined by the terms of the Withdrawal Agreement and Political Declaration, the UK's GDP in 2023 would be between 1.25% and 3.75% lower than it would have been if it had followed its pre-referendum trend. Under a scenario with no deal and no transition period, GDP would be between 7.75% and 10.5% inferior, and an immediate drop of between 3% and 8% was considered.

According to the many studies that have sought to quantify the economic effects of Brexit, it is quite unlikely that these negative effects will be offset in the long term (see Table 1). Admittedly, the results of these studies vary significantly, given their scope (some focus only on trade, others factor in foreign direct investment, migration, the UK's contributions to the EU budget, etc.) and the range of scenarios covered (the UK staying in the single market, leaving with a free-trade agreement, leaving without a deal, etc.). Nevertheless, they all agree on two important points. First, they are unanimous in concluding that, regardless of its final form, Brexit will have a negative effect on the UK economy. The second shared finding is that the "harder" the type of Brexit, the greater the shock to the UK economy will be. In fact, the shortfall is generally expected to be twice as large in the scenario of a no-deal Brexit, compared to a deal scenario – the two outcomes that remain on the table. According to a study from UK in a Changing Europe[6], the negative impact of a no-deal exit in the long term would be two to three times larger than the impact of the Covid-19 crisis.

In the long term, the consequences of Brexit for investment, productivity, potential growth and migration could also have a significant effect on the British economy. The Centre for Economic Performance[7] and the OECD[8] predict a drop in foreign direct investments (FDI) towards the UK of 22% and 30%, respectively, over a ten-year horizon. One explanation for these declines is that the UK has so far attracted investments thanks to the access it provided to the EU market. Meanwhile, research from the OECD as part of its latest Economic Survey for the UK[9] suggests that the increase in barriers to trade and to competitiveness could reduce the productivity of most UK service sectors by 3% to 5% over the long term.

Overall, these studies suggest that the impact of Brexit on the UK economy over the long term will depend on two key parameters: the initial shock caused by the end of the transition period and the degree of divergence between the UK and the EU. Whatever happens, it appears that the impact of Brexit on the UK economy will be negative, which could warrant fiscal and monetary support measures (see final section).

2 IoD responds to PM's Brexit statement warning businesses to prepare, Institute of Directors, October 2020.
3 Letter from Michael Gove to road haulage groups, Road Haulage Association (RHA), September 2020.
4 HM Treasury, *HM Treasury Analysis: The immediate economic impact of leaving the EU*, Discussion paper (May), London, 2016.
5 EU withdrawal scenarios and monetary and financial stability, Bank of England, November 2018.
6 Menon A, J. Portes, J. Rutter et al., *What would no deal mean?, UK in a Changing Europe and LSE*, September 2020.
7 Dhingra S., G. Ottaviano, T. Sampson, and J. Van Reenen, *The impact of Brexit on foreign investment in the UK*, Centre for Economic Performance (LSE), April 2016.
8 Kierzenkowski R., N. Pain, E. Rusticelli, and S. Zwart, *The Economic Consequences of Brexit: A Taxing Decision*, OECD Economic Policy Papers, No. 16, OECD Publishing, Paris, 2016.
9 OECD Economic Surveys: *United Kingdom 2020*, OECD, 2020.

ESTIMATED EFFECTS OF BREXIT ON UK GDP (DEVIATIONS FROM REMAIN SCENARIO)				
Study	**Date**	**EEA**	**FTA**	**WTO**
Booth et al. (Open Europe)	March 2015	-	-0.8%	-2.2%
PwC/CBI	March 2016	-	-1.2%	-3.5%
HM Treasury	April 2016	-3.8%	-6.2%	-7.5%
Kierzenkowski et al. (OECD)	April 2016	-	-5.1%	
Ebell & Warren (NIESR)	May 2016	-1.8% -	-2.1% with productivity:	-3.2% -7.8%
Rojas-Romagosa (CPB)	June 2016	-	-3.4%	-4.1%
Jafari & Britz	June 2017	-	-	-4.6%
Felbermayr et al. (IFO)	June 2017	-0.4%	-0.6%	-1.7%
Pisani & Caffarelli (Banca d'Italia)	January 2018	- -	-0.9% with productivity:	-2.0% -10.6%
Latorre et al.	June 2018	-1.2%	-	-2.6%
Vicard (CAE)	July 2018	-0.8%	-2.2%	-2.7%
IMF	July 2018	-	-2.5%	-4.0%
Hantzsche et al. (NIESR)	November 2018	-	-3.9%	-5.5%
Levell et al. (CEP)	November 2018	- with productivity:	-1.9% -5.5%	-3.5% -8.7%
UK Government	November 2018	- -	- with migration :	-7.7% -9.3%
Ortiz & Latorre	December 2018	-0.5%	-	-1.1%
Menon et al. (UKinEU)	September 2020	-	-	-8.0%
Arriola et al. (OECD)	Forthcoming	-	-3.5%	-

TABLE 1

SOURCE: SEE APPENDIX

The consequences of Brexit by economic sector

The consequences of Brexit will vary markedly across sectors, in part because of their different degrees of integration in international value chains. In boxes 1 and 2 (see pages 16 & 17), two typical cases are studied, the fishing sector and the aerospace industry. They illustrate the challenges of leaving an economic area as complex as the EU's single market.

More broadly, some sectors of the UK economy appear more vulnerable than others to Brexit. One reason is the relative importance of the EU market for each sector. The share of UK exports going to the EU varies significantly across sectors, from less than 20% in the case of insurance to more than 70% for communications and agriculture[10] (see Chart 1).

That being said, exports represent only a share of the total production of each sector. The share of exports going to the EU in the total production of each sector certainly gives a more precise idea of their reliance on the single market. Chart 2 shows that electronics, the primary sector, motorised vehicles and chemical products are the sectors that export the biggest share of their production to the EU – more than 20% in each case. By contrast, the communications sector has in fact little exposure to the single market. That is because, while 70% of the sector's exports are directed towards the EU, less than 5% of its production is exported.

Beyond exchanges, other factors, such as their degree of openness and structural differences, suggest that the impact of Brexit will vary substantially across sectors. A forthcoming study from the OECD[11] seeks to estimate the impact of Brexit on the UK's imports and exports by sector. It is based on the OECD's computable general equilibrium (CGE) METRO model, which incorporates developments in non-tariff measures, services trade and trade in value added. In the relatively favourable scenario where a free-trade agreement is found, the study estimates that, for each sector, imports will be roughly 5% to 10% lower over the medium term than they would have been if the UK had remained in the EU. When it comes to exports, all sectors would lose, with the exception of natural resources. The two sectors most affected, with losses of around 15%, would be motor vehicles and textiles (Chart 3). Under a no-deal scenario, exports would be reduced for all sectors, with shortfalls of more than 40% for motor vehicles and meat.

Overall, the manufacturing industry and agribusiness appear to be the most vulnerable to the UK's withdrawal from the EU's single market. However, it will probably be the services sector that will weigh the most on the UK economy. That is due to this sector's weight in the UK economy: services account for around 80% of total added value in the UK.

The impact on economic policy

Brexiteers argued during the campaign of the 2016 referendum that leaving the EU would lead to significant savings, as Brexit would end UK contributions to the EU budget. Between 2014 and 2018, the UK's average gross contribution was GBP13.4bn per year, when taking into account an average rebate equivalent to GDP4.6bn. Meanwhile, the EU provided funds to the UK public and private sectors amounting an annual average of GBP5.6bn – most notably under the Common

10 Latorre M. C., Z. Olekseyuk, H. Yonezawa, and S. Robinson, *Brexit: Everyone Loses, but Britain Loses the Most*, Working Paper Series WP19-5, Peterson Institute for International Economics, 2019.

11 Arriola C., S. Benz, A. Mourougane, and F. Van Tongeren (forthcoming), T*he Trade Impact of the UK's Leaving the EU Single Market*, OECD Economics Department Working Papers, OECD Publishing, Paris.

CHART 1 — SOURCE: PIIE, GTAP, FMI, BNP PARIBAS

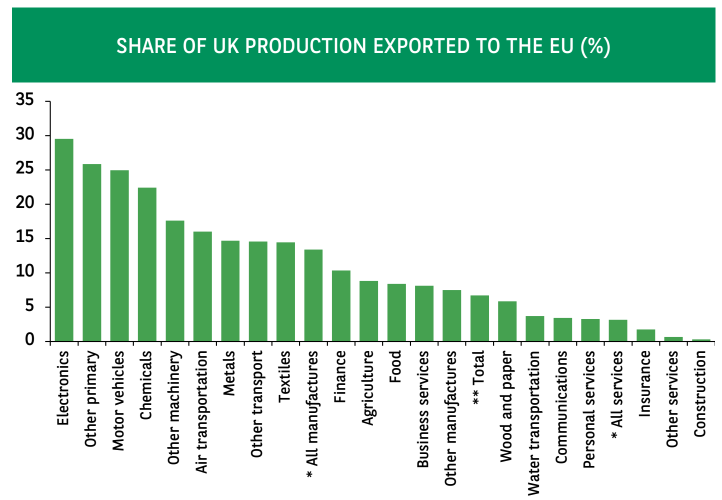

CHART 2 — SOURCE: PIIE, GTAP, FMI, BNP PARIBAS

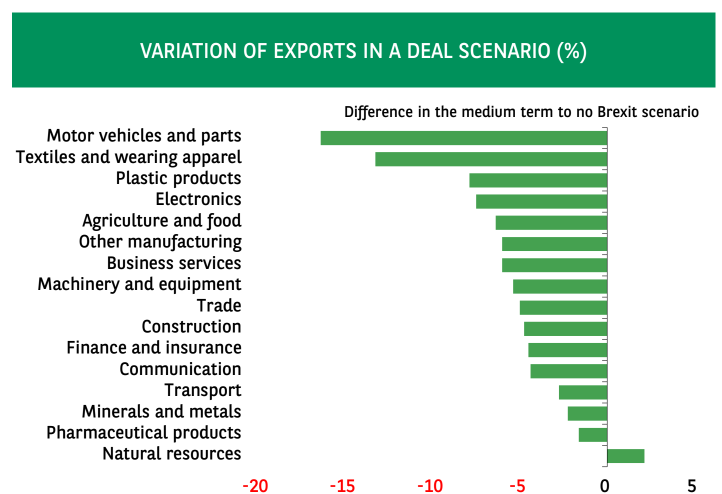

CHART 3 — SOURCE: OECD, ARRIOLA ET AL. (FORTHCOMING)

Agricultural Policy (CAP) and the European Regional Development Fund (ERDF). Overall, the UK's average net contribution was GBP7.8bn per year, which represents around 1% of total government spending[12]. As well as stopping its contributions to the EU budget, the UK will, as a result of its exit from the customs union, retain the revenues from the tariffs charged on its imports. Until now, these were transferred to the EU. While on the paper it seems that the UK will gain from Brexit, things might be quite different in reality.

First, any gains from the end of contributions will be limited over the coming years by the financial settlement. The settlement represents the UK's commitments undertaken prior to Brexit that the country will have to honour, and it is expected to exceed GBP30bn[13]. What's more, if they had been kept by the British government last year, the revenues from tariffs would only have added 0.4% to its total revenues. Lastly, and perhaps more importantly, the economic losses caused by Brexit will probably weigh on the UK's public finances, by dragging down government tax revenues and raising spending in some areas (such as unemployment benefits). This would raise the government's deficit – which has already increased markedly due to the Covid-19 crisis – and in turn government debt. Admittedly, the government could seek to counter this shock, but such support would take the form of some combination of additional expenditure and tax cuts. Therefore, a deterioration of the UK's public finances, relative to a scenario in which the country remained in the EU, appears inevitable.

Finally, it is also possible that the UK will seek to relax its regulations in order to attract investors and businesses. However, the UK is already one of the most lightly regulated developed economies, particularly in terms of labour protection and product market regulation. On top of this, any regulatory divergence from the EU would presumably be followed by additional barriers to trade with the EU, as the latter pays particular attention to ensuring that access to its market meets strict conditions in order to maintain fair competition.

When it comes to monetary policy, the Bank of England remains pragmatic. In a speech to the Central Bank of Ireland in September 2018[14], Mark Carney, the then Governor of the Bank of England, noted that the monetary policy response was not automatic and would *"depend on the balance of the effects on demand, supply, and the exchange rate"*. The central bank is concerned that it will face the scenario it confronted in the immediate aftermath of the referendum. On the one hand the fall in the pound had created inflationary risks, and on the other hand the uncertainty triggered by the result of the referendum had raised fears of a significant economic slowdown. Faced with this dilemma, the Bank of England ultimately decided to ease monetary policy, notably by cutting its policy interest rate by 25 basis points to 0.25% and by expanding its quantitative easing (QE) programme.

The Bank of England could face a similar situation after the UK's effective withdrawal from the EU. A no-deal scenario would quite likely lead to a depreciation of the pound, considering the uncertainty it would generate. A significant depreciation would correspond to an easing of financial and monetary conditions – via its effect on export competitiveness – and hence soften the blow to the economy. However, it would also create upward pressures on inflation via higher import prices. Nevertheless, in this scenario, the Bank of England would probably still opt for looser monetary policy.

Monetary support could come in the form of zero or even negative interest rates – Bank Rate has already been cut to a record low of 0.10% following the Covid-19 crisis. To this end, the Bank of England has conducted a survey[15] to assess the financial sector's readiness for a hypothetical introduction of zero or negative rates. Although the central bank denied that this survey was indicative that such policy would eventually be adopted, money markets are already pricing in a fall in interest rates to negative levels in the coming months.

Otherwise, the Bank of England could expand its QE programme further. However, the share of government bonds it owns has significantly risen with the Covid-19 crisis. While at the beginning of the year the central bank was targeting a stock of GBP425bn in sovereign bond purchases, it has since raised this figure to GBP875bn. At present, the bank holds nearly 45%[16] of outstanding government bonds. It is true that the central bank can own up to 70% of the "free float" – which is the total amount in issue minus government holdings. However, given the large share the central bank already possesses, the effects of more purchases would be uncertain. Moreover, the Monetary Policy Committee (MPC) could be unwilling to increase the share of sovereign bonds it holds much further. When a central bank detains a substantial share of its own government's debt, the line between independent policy and monetary financing – the direct financing of the government – becomes blurred, which could potentially damage the central bank's credibility. Nevertheless, the Bank of England has more scope when it comes to purchases of corporate bonds. One reason is that such purchases do not incur the risk of monetary financing. Another is that, although the Bank of England has doubled its target for corporate bond purchases since the crisis began, the target is now at GBP20bn, which represents only around 10% of the total stock of eligible bonds. This suggests that the bank has more leeway in this area, which could prove particularly useful given that British companies risk bearing the brunt of the negative effects caused by Brexit.

Conclusion

Overall, in light of the unprecedented nature of the UK's decision to leave the European Union, there is considerable uncertainty around its consequences, although no study expects the country to benefit from it. Given the UK's choice to leave both the EU's single market and customs union, this will surely be a hard Brexit. Although a free trade agreement would prevent the imposition of tariffs and quotas, numerous non-tariff barriers will emerge in any case and entail a cost for the British economy. It will take time and money for companies – in particular those which are not well prepared – to adapt to the changes. While the UK's fiscal and monetary authorities could attempt to offset the short term impact through more accommodating policies, the Covid-19 crisis has reduced their room for manoeuvre.

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12 The UK contribution to the EU budget, Office for National Statistics (ONS), September 2019.
13 *Brexit: the financial settlement – in detail*, UK Parliament, March 2020.
14 "The future of work", speech by Mark Carney, Bank of England, September 2018.
15 Letter from Sam Woods 'Information request: Operational readiness for a zero or negative Bank Rate', Bank of England, October 2020.
16 Bank of England faces new doubts over potency of buying bonds, Financial Times, 3 November 2020.

FISHERIES: SMALL SECTOR BUT BIG DISAGREEMENTS

Despite being a minor sector for the British economy – its value added accounted for only 0.1% of GDP in 2019 – the UK fishing industry has been a key issue in the negotiations between the UK and the EU on a free-trade agreement. Given that European fishermen are highly dependent on their access to British territorial waters, the UK benefits from real leverage on this issue.

The Common Fisheries Policy

At the European level, the fishing industry is regulated by the Common Fisheries Policy (CFP), which was introduced in 1970 and reformed in 2014. The CFP gives the entire European fleet equal access to the territorial waters of all member states. It has four main policy areas: managing fisheries, with the aim of safeguarding stock reproduction, laying the foundations for a profitable industry, sharing out fishing opportunities fairly, and conserving marine resources; developing and implementing policy at the international level; managing the market in fishery and aquaculture products; and the funding of the policy which, for 2014-2020, is organised through the European Maritime and Fisheries Fund (EMFF). As part of its role of managing fisheries, the CFP sets common rules for all fishermen on which species can be caught, where they can be caught, how much can be caught, and with what equipment. The CFP seeks to establish sustainable fisheries and to preserve stocks, notably by including bycatch in the quotas allocated to each fisherman.

What is the UK offering?

The British fishing industry considers the CFP unfair and has for many years criticised its unilateral nature. When only considering volumes taken, free access to the EU's territorial waters does benefit more to EU fishermen than to their UK counterparts. Between 2012 and 2016, for example, an average of 760,000 tonnes of fish, worth around GBP540mn, were caught by vessels from other EU members in British waters, while the UK fleet caught only 90,000 tonnes, worth GBP110mn, in EU territorial waters[1].

What's more, the CFP subjects UK fishermen to strict quotas. As a result, the volume of fish taken by the British vessels in their own waters has halved since the introduction of the policy. London also criticises the arbitrary manner fishing quotas are allocated. For instance, in the Channel, French boats are allowed to take nearly nine times more cod than UK fishermen – although in UK waters overall British vessels take nearly three quarters of the cod.

The central issue in the negotiations regarding fisheries therefore lies in the extent to which the UK will regain control of its territorial waters. Given that the UK will no longer be constrained to allow EU fishermen into its waters, Michael Gove has called for greater realism and flexibility from the European negotiators.

What is Brussels asking for?

On the European side, Michel Barnier was until recently demanding full access to UK territorial waters for EU fishermen. This position was mainly backed by France, Belgium, the Netherlands and Spain. Fisheries primarily concern eight European countries, but all twenty-seven remaining EU members have remained united on the issue.

Access to British waters is vital for the fleets of many of the UK's neighbours, notably Belgium. With just 67km of coastline, Belgium has a very limited Exclusive Economic Zone. As a result, 80% of the 15,000 tonnes of fish sold each year in the country's two biggest fish markets, Ostend and Zeebrugge, come from British waters, and 4,200 jobs depend directly on the fishing industry.

The UK's proposal that any agreement should be renegotiated every year – on the same model as the agreement between the EU and Norway – was staunchly opposed by the Europeans, who feared lack of stability for their fishermen. The Europeans have also refused to separate fisheries from the overall negotiations with the UK. In response, Boris Johnson has threatened to leave the EU without a deal.

What would happen if no deal is found?

Should no agreement be reached between the two parties, WTO rules would apply, which would mean the introduction of customs checks and the application of tariffs. The UK could even deny European vessels access to its territorial waters, where they find 42% of their total catch volumes each year. Indeed this figure is even higher for the fleets of the UK's closest neighbours, such as the Netherlands and Belgium. According to the European Fisheries Alliance, this ban could cut the profits of European fleets by half and result in the loss of 6,000 jobs[2]. A lack of agreement on fisheries would also lead to more administrative procedures – such as authorisations for the sale of their products – for many fishermen who currently land their catches freely in UK ports.

Meanwhile, in a no-deal scenario, UK fishermen and dealers would see restrictions on their access to the territorial waters of the EEA and, more importantly, to the single market. In particular, tariffs would be charged on their exports of fish to the EU – the rate applied by the EU to fish and fish products is nearly 12%. Given that 75% of UK fisheries exports go to the European market, this would certainly have a severe effect on the UK fishing industry. Finally, failure to reach an agreement, particularly on quotas, would raise the risk of overfishing.

Faced with these prospects, the UK government is attempting to reduce the country's dependence on the European market by negotiating bilateral agreements not only with EU member states but also with third countries such as Norway.

1 Sustainable fisheries for future generations, Department for Environment, Food and Rural Affairs, July 2018
2 Building a sustainable, strong and mutually beneficial joint Fisheries Management post-Brexit, European Fisheries Alliance, January 2020.

BOX 1

AEROSPACE, A BIG MISSING PIECE IN THE NEGOTIATIONS

"In the event of a no-deal Brexit, Airbus would have to make some decisions that would be very painful for the UK." This was the message to the UK from Tom Enders, former CEO of Airbus, in January 2019. A year later, his successor, Guillaume Faury, stated his determination to work with the UK on "an ambitious industrial strategy", and said that he foresaw "significant potential to improve and expand" Airbus' activities in the United Kingdom, suggesting increased awareness of the importance of this market for the company's business model.

The UK aerospace industry

The aerospace sector is a key pillar of the UK's economy and accounts for roughly 114,000 jobs. In 2019, this industry alone generated GBP34 billion in value added, which is equivalent to 7% of total industrial value added. The sector is one of the strongest growing in the UK and is associated with very high productivity per head.

At present, the UK is an important piece of the Airbus production line, supplying the company with components such as wings, engines and landing gear, which are then assembled in EU countries – most notably France. As a result, in 2018 half of the UK's exports of aerospace parts and components by value went to EU member states.

How is the industry structured at the European level?

The EU aerospace industry is fully integrated and regulated by the European Aviation Safety Agency (EASA). EASA is one of the only two organisations that is allowed to certify aerospace parts, components and products – the other being the US Federal Aviation Administration (FAA). Manufacturers active in the UK, such as Airbus, Rolls Royce, GKN and Bombardier, therefore rely on EASA certification. Countries that are not members of the EU can become associate members of the EASA. While this allows them to benefit from EASA agreements and certification, they do not have voting rights. Thanks to the Bilateral Aviation Safety Agreement (BASA), EASA members enjoy access to the markets of a number of third countries, such as the USA, Brazil and Canada.

As the transition period nears its end, uncertainty remains

If no deal is found between the EU and the UK, the latter will leave EASA on 1 January 2021. This would have immediate negative consequences for the UK aerospace industry.

First, this would prevent the certification of aerospace components produced in the country. A transition period lasting several years would certainly have to be put in place before the British Civil Aviation Authority (CAA) could be able to assume this certification role.

The UK exiting the EASA would also result in customs checks at its borders with the EU. According to the ADS business federation, this would represent additional costs of GBP1.5 billion per year for the aerospace sector. Indeed, as far as the aerospace sector is concerned, trade between the UK and EU is very intensive. For example, the delivery time for wings from Airbus' Broughton production site to its Toulouse assembly centre is currently only two hours, and several trips can be made each day with no administrative requirements[1].

Lastly, leaving the EASA would mean for the UK being cut off from the markets of third countries with which the agency has bilateral agreements.

That said, in a no-deal scenario the UK would still be covered by the WTO agreement on aerospace products and components, which means that no tariffs would be applied to civilian aircraft products and components. Whilst this agreement does not cover intermediate products and raw materials, these are nevertheless protected by a specific regime adopted by the EU, from which UK exporters would continue to benefit.

Faced with these prospects, one of the options considered would be to keep the UE in the EASA as an associate member. The UK would no longer participate in the EASA's decision process, but would continue to benefit from its bilateral agreements. In any case, Mr. Faury notes that "numerous precautions" will have to be taken by governments to protect European aerospace value chains.

1 According to evidence given by Katherine Bennett, Senior Vice-President at Airbus UK, during a House of Lords Committee in 2017.

BOX 2

APPENDIX: SOURCES FOR TABLE1

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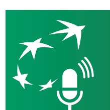

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