HOUSE OF COMMONS LIBRARY

BRIEFING PAPER

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End of Brexit transition period: Economic impact

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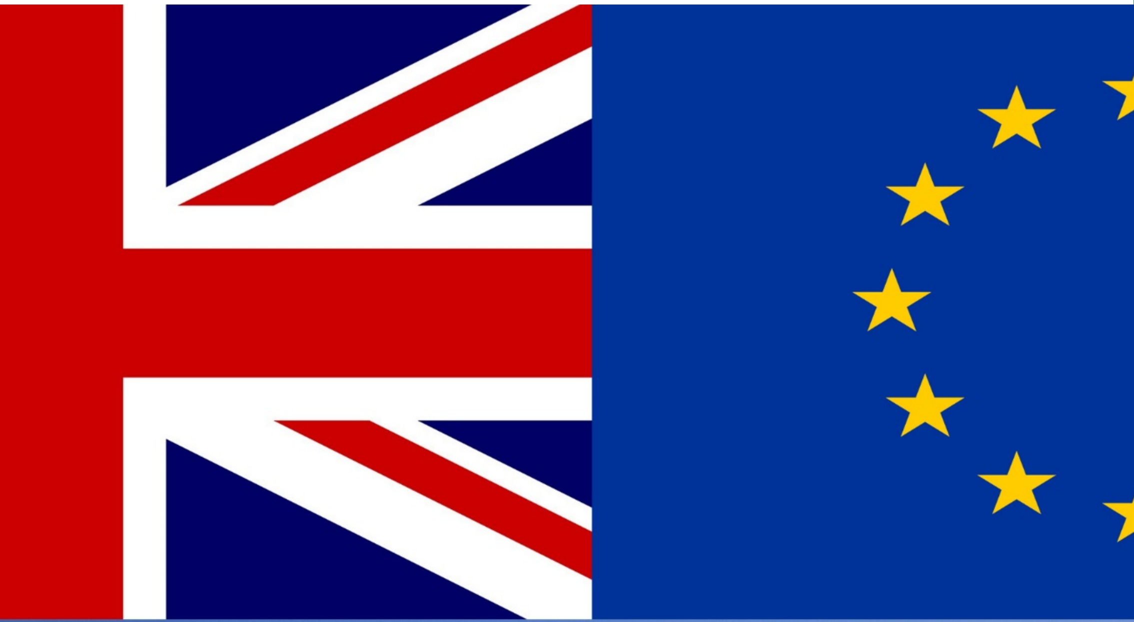

Contents:

Contents

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Summary

The UK is scheduled to leave the Brexit transition period, and thereby the EU's single market and customs union, on 1 January 2021. This will result in the nature of the UK-EU economic relationship changing, whether the UK and EU agree a free trade agreement (deal scenario) or not (no-deal scenario). In turn, this will impact the UK economy, as the EU is, by far, the UK's largest trading partner.

The short-term impact in deal and no-deal scenarios

In the short term, additional trade frictions between the UK and EU will occur in both scenarios. There is also the possibility of immediate disruption to trade from 1 January 2021 due to the new rules with, for example, new border checks and customs formalities.

There will, however, be additional trade frictions in a no-deal scenario, such as tariffs on some goods. Prominent economic forecasters expect weaker economic growth if there is no trade agreement. The Office for Budget Responsibility (OBR), for example, expects UK GDP to be 2% lower in 2021 under a no-deal scenario compared with a deal scenario.

The long-term impact in deal and no-deal scenarios

Brexit is likely to lead to a long-term structural change in the UK economy, impacting areas such as trade, investment and immigration.

The vast majority of economic studies from the government (in 2018) and others show that the higher the barriers (cost) of trading with the EU (via tariffs and non-tariff barriers), the larger the negative impact on the UK economy overall in the long-term. A no-deal outcome is associated with a greater hit to GDP.

The OBR, based on analysis of external economic studies, expects UK GDP to be around 4% lower in a deal scenario in the long-term compared to a scenario where the UK stayed in the EU. In a no-deal scenario the OBR expects GDP would be an additional 2%-points lower.

Uncertainty is high

There is a high degree of uncertainty surrounding such estimates and the economic outlook in general, not least due to the ongoing pandemic.

1. UK-EU economic relationship to change from 2021

The UK left the EU on 31 January 2020 under the terms of the Withdrawal Agreement.[1] Since then, the UK has been in a 'transition period' with the EU. During this time, the UK has remained in the EU's single market and customs union, ensuring the economic relationship has stayed essentially unaltered.

With the transition period scheduled to end on 31 December 2020, this will change. If the UK and EU fail to agree a new deal on their future relationship, the default position will be that UK-EU trade will be based on World Trade Organization (WTO) rules. This is often described as a **no-deal scenario** and this term will be used in this briefing.

If the UK and EU come to an agreement, the terms of the deal will shape their future economic relationship, including on the crucial areas of trade and investment. The term **deal scenario** will be used in this briefing for such a situation.

At the time of publication (18 December), it was unclear whether an agreement would be reached.

Under both deal and no-deal scenarios, the nature of the UK-EU economic relationship will change from what it is currently (and from when the UK was an EU member state).

The **EU collectively is, by far, the UK's largest trading partner**.[2] The terms of a deal, or the absence of one, will therefore play a large role in determining the economic impact of Brexit. There have been many economic studies over recent years that have sought to quantify this.[3] These have tended to focus on the long-run effects. In addition, more recent economic forecasts have provided estimates of the potential short-term impact of deal and no-deal scenarios.

This briefing provides an overview of possible short- and long-term economic impacts resulting from both deal and no-deal scenarios. There is a **high degree of uncertainty** surrounding such estimates and the economic outlook in general, not least due to the ongoing pandemic.

The briefing focuses on the impact of the change in the overall UK-EU economic relationship due to Brexit. In respect to trade, this is mostly based on the relationship between Great Britain and the EU. Comments in this briefing refer to GB-EU trade. Separate arrangements apply to trade between Northern Ireland and the EU (under the Protocol on Ireland/Northern Ireland in the Withdrawal Agreement).

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1 HM Government, New Withdrawal Agreement and Political Declaration, 19 October 2019

2 Commons Library Briefing Paper (Nov 2020), Statistics on UK-EU trade

3 See Office for Budget Responsibility (Oct 2018), Discussion paper No.3, Brexit and the OBR's forecasts, and Institute for Government (Oct 2018), Understanding the economic impact of Brexit

2. Short-term economic impact

The nature of the UK-EU economic relationship will change following the transition period. This will be most visible in higher barriers to trade. The short-term impact will depend to some extent on whether there is a UK-EU trade deal or not. However, as the UK will leave the EU single market and customs union is both scenarios, there will be additional trade frictions between the UK and EU regardless.

There is also the possibility of immediate disruption to trade from 1 January 2021 due to the new rules with, for example, new border checks and customs formalities.

2.1 Short-term factors

Channels through which the economy may be affected in the short term, in both deal and no deal scenarios, include:

- **Potential border disruption** – businesses need to adjust to new rules and regulations for UK-EU trade, with new paperwork and customs procedures. If there is a trade deal, this will be less burdensome than under a no-deal scenario. In addition, there may be more goodwill in implementing new border controls if there is a deal. The degree of disruption will depend on how prepared businesses are, as well as the administrative and operational readiness of UK and EU authorities to ensure minimal disruption at the border.[4]
- **New barriers to UK-EU trade** – there will be additional costs to UK-EU trade. This is likely to result in lower amounts of trade flowing between the UK and EU than would be the case if the UK remained in the customs union and single market. For example, it seems very likely that it will be harder for many UK companies to export their services to EU clients. How high these additional barriers are will be determined by the terms of any deal and will be highest if there is no deal.[5]
- **Uncertainty** – with the terms of UK-EU trade from 1 January 2021 unclear weeks before there has been a high degree of uncertainty facing UK firms that trade with the EU. It can be argued this uncertainty has been prevalent to some degree since the EU referendum of June 2016 and has negatively affected business investment.[6] Should a trade deal be agreed, some or much of the Brexit-related uncertainty may be lifted (although there may still be a period of getting used to the new rules).
- **The value of sterling** – pound sterling exchange rates with foreign currencies may move in response to whether there is a free trade deal or not. In the case of no deal, most economists

[4] Bank of England, Monetary Policy Report, 5 November 2020, section 4
[5] For more see Commons Library briefing paper (Dec 2020), End of Brexit transition: trade
[6] OBR, Economic and fiscal outlook: March 2020, pp.26-28, Box 2.1, and para 2.32

expect the value of the pound to fall.[7] The pound fell sharply following the result of the EU referendum and has not recovered its previous level. This resulted in higher import prices, rising inflation and lower real (inflation-adjusted) average household disposable incomes.[8] What actually happens in a deal or no deal scenario is difficult to be certain about given the inherent difficulty in predicting foreign exchange movements.

- **Interaction with coronavirus economic impact** – how will the ongoing pandemic interact with the factors mentioned above? The immediate potential border disruption linked to Brexit may be exacerbated by global transportation issues related to the pandemic.[9] On the other hand, if lower-than-normal volumes of trade, tourism and immigration continue due to the pandemic this may help free up some capacity to ease any Brexit-related disruptions.[10]

2.2 The short term in a deal scenario: UK-EU free trade agreement

The vast majority of economic forecasts for 2021 and beyond are based on the assumption that the UK and EU negotiate a free trade agreement (FTA). This includes those from the Bank of England and the Office for Budget Responsibility (OBR), the UK's independent fiscal watchdog.

The coronavirus pandemic has resulted in sharp swings in economic conditions and data, most notably GDP growth.[11] As a result, effects from the pandemic swamp expectations of any Brexit-related impacts in 2021. For example, GDP is expected to have declined by over 10% in 2020.

A recovery from this historically large fall is expected to lead to growth of over 5% in 2021, well above the 'normal' range of the UK annual GDP growth rate.[12] This will make it more difficult to see the Brexit impact in headline economic data.

Assumptions of a free trade deal are already embedded in most economic forecasts; this means they have already taken into account the impact of higher UK-EU trade barriers resulting from the UK leaving the EU's single market and customs union.

It is already possible to produce these forecasts, even without the details of a deal, because the economic models used to make these forecasts are not generally influenced by every specific element of a trade deal; rather an assumption of the overall shape and scope of a trade deal is

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[7] OBR, Economic and fiscal outlook: November 2020, p.198, para B.13
[8] Thomas Sampson, LSE blog, Higher inflation, lower wages and decreasing output: Brexit is starting to negatively affect the UK economy, 10 July 2018
[9] Institute for Fiscal Studies, Green Budget: chapter 3 'The cost of adjustment: emerging challenges for the UK economy' (authored by Citi), October 2020, p.148
[10] UK in a Changing Europe, What would no deal mean?, September 2020, p.55
[11] Commons Library briefing paper (December 2020), Coronavirus: Economic impact
[12] HM Treasury, Survey of independent forecasts for the UK economy, 16 December 2020

used. So, for example, forecasters might assume a 'standard' trade agreement with higher barriers to UK-EU trade rather than a more comprehensive one which involves lower barriers to trade.

Bank of England forecasts

In November, the Bank of England's Monetary Policy Committee released its latest assessment of the UK economy. The Bank forecast that **GDP will be around 1% lower than it otherwise would be in Q1 2021** as a result of businesses adjusting to new trading arrangements.[13]

Specifically, the Bank expects lower UK exports to the EU. This is a consequence of some firms not being fully prepared for new customs and document checks at the border. (The Bank assumes the EU will apply full customs and border controls from 1 January 2021.)

The impact is seen as being temporary and is expected to unwind over six months as businesses adjust.[14] The Bank's forecast is based on a UK-EU trade deal of "similar scale and depth" to the EU-Canada deal.[15]

Over a longer time period, the Bank of England expects trade in goods and services to be lower under a deal scenario than if the UK remained in the single market and customs union. Citing empirical evidence, it expects this reduction in trade with the EU to "weigh on productivity and GDP" over the next few years.[16]

Office for Budget Responsibility

The OBR must base its main forecasts on government policy, which is to reach a trade deal with the EU. In its November 2020 forecasts, the OBR did not include a specific negative impact from possible border disruption in early 2021 (unlike the Bank of England, as discussed above), though it does note that this is a "downside risk" to its forecasts.[17]

The OBR has also provided some estimates of what it expects the overall economic impact of Brexit will be on the economy in the long term (see section 3.3 below for more). Based on a free trade agreement, it expects GDP to be 4% lower in the long run compared with remaining in the EU.[18] The OBR has said that around one-third of that 4% has already occurred.[19] In other words**, the OBR estimates that the impact of Brexit to date is to lower GDP by around 1.4%**. This is mainly a result of weaker business investment.[20]

[13] Bank of England, Monetary Policy Report, 5 November 2020, pp.3-4 and pp.41-42
[14] Bank of England, Monetary Policy Report Press Conference, 5 November 2020, p.10
[15] Bank of England, Monetary Policy Report, 5 November 2020, p.3
[16] Bank of England, Monetary Policy Report press conference: opening remarks by Andrew Bailey, Governor, 5 November 2020
[17] Office for Budget Responsibility, Economic and fiscal outlook: November 2020, p.29, para 2.11
[18] Ibid.
[19] OBR budget responsibility committee member Prof Sir Charlie Bean, Oral Evidence to Treasury Committee, 1 December 2020, Q46
[20] OBR, Economic and fiscal outlook: March 2020, pp.26-28, Box 2.1, and para 2.32

Other assessments

In October 2020, **Citi**, the investment bank, provided forecasts and analysis for the Institute for Fiscal Studies' annual *Green Budget* report.[21] Citi estimated that under a 'thin', or limited, UK-EU trade deal UK GDP in 2021 would be 2.1% below what it would be if the UK remained in the single market and customs union. By the end of 2024, Citi estimated GDP would be 1.4% lower.[22]

In its October 2020 assessment of the UK economy, the **OECD** observed that even under a comprehensive UK-EU deal there would be a number of additional frictions to UK-EU trade from 2021:

> Even assuming a comprehensive accord, there will be rising technical barriers and sanitary and phytosanitary measures and a lower level of trade facilitation on goods as well as increased non-tariff barriers on services, as regulations between the United Kingdom and the European Union diverge over time. In addition, rules-of-origin requirements will need to be put in place to determine whether goods qualify for tariff-free entry. UK exports will thus face much higher compliance costs stemming from increased customs checks and border delays.[23]

2.3 The short-term in a no-deal scenario: WTO terms

As discussed above, under a no-deal scenario there will be additional barriers to UK-EU trade compared with a deal scenario. In the short-term, this could lead to greater border disruptions, increase uncertainty and may result in a decline in the value of the pound. The magnitude of the short-term impact is uncertain, particularly as it would occur against the backdrop of the ongoing effects from the pandemic.

As most economic forecasts assume that a trade agreement is reached, some economists have presented additional analysis of a no-deal scenario. The results from prominent organisations **generally forecast GDP to be 1-2% lower over the next few years in a no-deal scenario compared with a deal scenario**. Some of these forecasts are summarised below.

Office for Budget Responsibility

In its November 2020 forecasts, the OBR published a no-deal Brexit scenario for the first time.[24] Its central forecasts (described in the previous section) are based on government policy, which is to negotiate a UK-EU trade agreement.

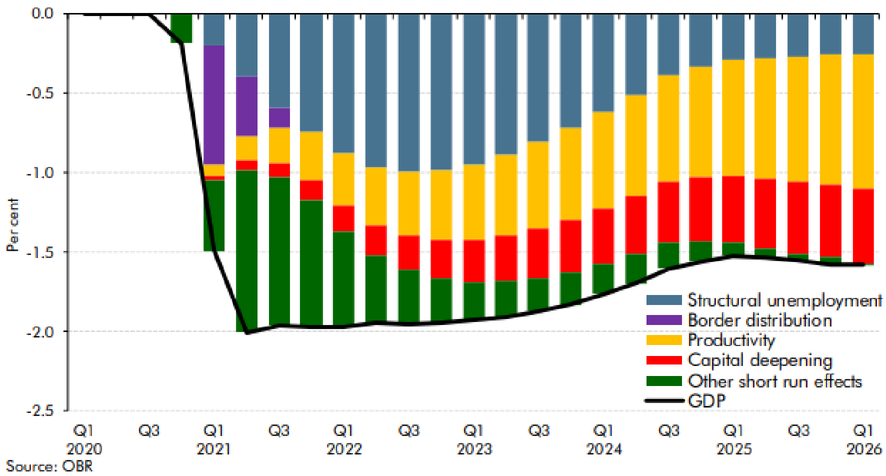
The OBR estimates that a in no-deal scenario, **UK GDP could be 2% lower than under a deal scenario in 2021**[25] due largely to temporary disruptions to trade. The OBR expects these to fade over time as businesses and governments get used to the new rules and procedures.

[21] Institute for Fiscal Studies, Green Budget: chapter 3 'The cost of adjustment: emerging challenges for the UK economy' (authored by Citi), October 2020
[22] IFS Green Budget, Chapter 3 (authored by Citi), October 2020, pp.150-151
[23] OECD, OECD Economic Surveys: United Kingdom 2020, October 2020, p.58
[24] OBR, Economic and fiscal outlook: November 2020, Annex B: Brexit scenarios
[25] OBR, EFO: Nov 2020, p.29, para 2.12

However, longer-term effects of lower trade start to have an effect, caused by higher barriers to trade, resulting in GDP being 1.5% lower after five years (early 2026).[26]

The chart below, taken from the OBR analysis, illustrates its GDP expectations in a no-deal scenario compared with a deal scenario (its central forecast).[27]

Chart B.2: Difference in real GDP to central forecast



Source: OBR

Under a no-deal scenario, the OBR estimates that the **unemployment rate** would peak 0.9%-points higher (at 8.3% in Q3 2021) than its central forecast under a deal scenario.[28]

The OBR expects the government **budget deficit** to widen in a no-deal scenario, due to lower economic activity (as measured by GDP). In a no-deal scenario the OBR expects the budget deficit to be on average 0.5%-points of GDP higher per year from 2021/22 to 2025/26 (the end of its forecasts).[29] In 2021/22, the budget deficit would be £12 billion higher than under a deal scenario.[30] Total public sector net debt would by 2.9% of GDP higher on average under a no-deal scenario in the five-year period from 2021/22.[31]

Other assessments

A selection of recent forecasts and analysis related to a no-deal scenario:

- **National Institute of Economic and Social Research (NIESR)** – estimates that GDP would be around ¾% lower by the end of 2021 compared with a deal scenario.[32] This gap gets larger to around -1% by 2023. It also notes that the sectors of the economy most likely to be impacted by a no-deal scenario

[26] The OBR does include estimates of largely continuity trade deals the UK has agreed with countries, such as Japan, that have trade deals with the EU. The OBR does not include potential FTAs with other economies such as the US, but it expects gains from such deals to be "modest" (see OBR, para B.9 for more detail)
[27] OBR, EFO: Nov 2020, p.197, chart B.2
[28] OBR, EFO: Nov 2020, pp.198-9, para B.14 and chart B.5
[29] OBR, EFO: Nov 2020, p.152, table 3.33
[30] OBR, EFO: Nov 2020, p.201, table B.3
[31] OBR, EFO: Nov 2020, p.152, table 3.33
[32] National Institute of Economic and Social Research, Prospects for the UK economy, 2 November, F8-9

appear to be different to those most affected by the pandemic (the pandemic particularly affects close-contact services, which often have less involvement in international trade).[33]

- **OECD** – warned, in its early December assessment of the global economy, of negative economic consequences of a no-deal scenario to the UK economy:

  > The failure to conclude a trade deal with the European Union by the end of 2020 would entail serious additional economic disturbances in the short term and have a strongly negative effect on trade, productivity and jobs in the longer term. By contrast, a closer trade relationship with the European Union than expected, notably encompassing services, would improve the economic outlook in the medium term.[34]

- **Citi** – October forecasts from the investment bank, provided for the Institute for Fiscal Studies' *Green Budget* report, expects GDP to be 0.5-1.0% lower in a no-deal scenario.[35] They state that if there is a deal, it would be a 'thin', not very wide-ranging, deal but there would still be additional implications of no deal:

  > …we [Citi] think most of the direct economic costs associated with Brexit are likely to materialise whether the UK leaves with a thin trade deal or with no deal at all. But leaving the EU without any deal at all would still impose additional costs, mostly via sentiment.[36]

- **UK in a Changing Europe** – the think tank described possible short-term economic impacts of a no-deal scenario, including the risk that EU-based businesses may seek to avoid UK suppliers. In addition, multinationals may try and minimise EU-UK border-crossings for its trade to avoid any border disruption.[37]

- **Bank of England** – has not presented a specific no-deal scenario recently. The Bank's Governor, Andrew Bailey, said the Bank's forecasts are "condition[ed] on government policy"[38] which is to have a trade agreement with the EU.[39]

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[33] See also Raoul Ruparel opinion column, "There's no hiding Brexit impact in coronavirus recession", Politico, 20 October 2020
[34] OECD, Economic Outlook, 1 December 2020, p.260
[35] Institute for Fiscal Studies, Green Budget: chapter 3 'The cost of adjustment: emerging challenges for the UK economy' (authored by Citi), October 2020, p.152
[36] Ibid.
[37] UK in a Changing Europe, What would no deal mean, September 2020, pp.54-56
[38] Bank of England, Monetary Policy Report Press Conference, 5 November 2020, p.10
[39] In late 2018, the Bank did publish analysis of different Brexit scenarios, including for no deal. These are summarised in Library briefing paper (Dec 2018), Brexit deal: Economic analyses.

3. Long-term economic impact

Brexit and the terms of the new UK-EU relationship will affect many different aspects of the UK economy, including trade and investment, immigration, regulations and EU budget contributions.

Brexit is likely to lead to a structural change in the UK economy. Higher trade barriers with the EU will likely result in a reallocation of economic resources, with potential consequences for certain industries and the economy overall.

The vast majority of previous economic modelling exercises from the government (in 2018) and others show that the higher the barriers (cost) of trading with the EU (via tariffs and non-tariff barriers), the larger the negative impact on the UK economy.[40]

3.1 Long-term factors

The main channels through which the UK economy may be affected over the long term in both deal and no-deal scenarios are:

- **Trade** – will play a crucial role in determining the long-term economic impact of Brexit. At present, the UK is in the EU single market and customs union ensuring very low barriers to trading with the EU. As the UK leaves, these barriers will increase, more so under a no-deal scenario. How trade with non-EU countries will evolve will also play a role in determining the overall impact on UK trade. Most economic studies show overall UK trade will be lower and this translates into a lower level of GDP compared with the UK staying in the EU.
- **Investment** – the UK is a leading destination for foreign investment. Being in the EU single market and customs union provides the opportunity for firms to trade with the EU with minimal trade barriers. Without this access, firms may see the UK as a less attractive destination for investment (and domestic firms may shift some of its output to be based in the EU). However, the UK's attractiveness as a location goes deeper than being part of the EU's economic network. The UK, for example, has flexible labour markets, a language spoken widely around the world, an educated workforce and a strong rule of law which are attractive for investors.[41]
- **Regulation** – depending on the terms of the future UK-EU relationship, the UK will have more control in setting regulations that are no longer subject to EU laws. The UK may therefore have scope to change business regulations, potentially in a way that boosts the economy, although this will be subject to domestic political debate and, in a deal scenario, the terms of

[40] See Office for Budget Responsibility (Oct 2018), Discussion paper No.3, Brexit and the OBR's forecasts, and Institute for Government (Oct 2018), Understanding the economic impact of Brexit

[41] London School of Economics, "Foreign investors love Britain - but Brexit would end the party", CentrePiece magazine, Summer 2016

the trade agreement (such as the level playing field provisions). Most economic studies find only limited potential economic gains from such freedoms.

- **Immigration** – by leaving the EU single market, freedom of movement will cease under deal and no-deal scenarios. Government immigration policy will play a large role in determining the economic impact of this in the long-term. The impact of the pandemic on immigration flows adds to the uncertainty over the economic impact.[42]
- **Public finances** – as an EU member state, the UK had been a net contributor to the EU budget, paying in more than it received from EU programmes. This payment was roughly equivalent to 0.4% of annual GDP.[43] The UK's financial settlement for leaving the EU was agreed in the Withdrawal Agreement and will not change in either a deal or no-deal scenario.[44] This payment will be lower than as an EU member state. The overall net impact on the public finances from Brexit will likely be determined by the wider impact on the economy rather than the direct savings from EU budget contributions. For instance, the larger the negative impact on economic activity (GDP), the lower tax revenues will be.

For a longer discussion of the impact of each of these factors please see section 1 of Library briefing paper (December 2018) Brexit deal: Economic analyses.

3.2 Economic impact assessments

Many economic studies have been conducted into the long-term economic effects of Brexit.[45] What the vast majority have in common is that they find that the looser the UK's future trading relationship with the EU, the larger the negative impact on UK GDP is.

These studies are different to the short-term forecasts discussed in section 2 of this briefing. These longer-term studies present a comparative analysis of how big the UK economy is – as measured by GDP – under scenarios such as deal and no deal compared to a 'baseline' scenario, usually of the UK remaining in the EU.

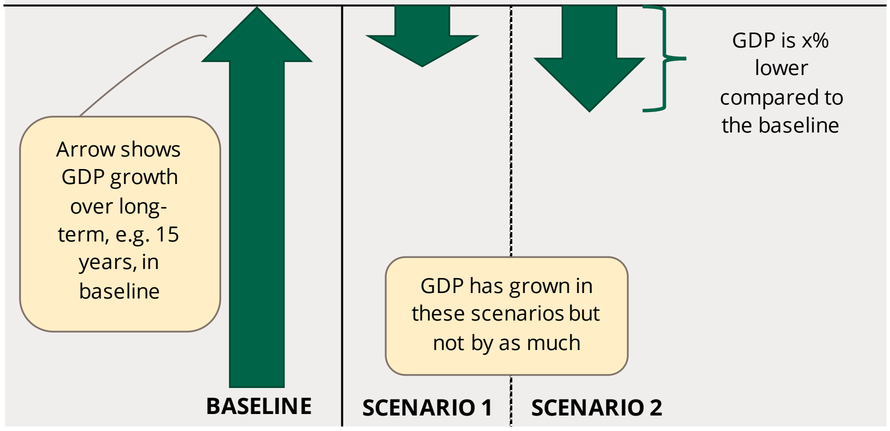
By longer-term they refer to when the economy has fully adjusted to the new situation and is in a 'steady state'. This is usually defined as 10-20 years. Each study will use its own estimates of potential trade costs and its own assumptions relating to how sensitive trade and GDP is to these changes in costs. Other assumptions will also be made and differ between studies.

[42] For more on the post-Brexit immigration system see IPPR, Building a post-Brexit immigration system for the economic recovery, November 2020
[43] Commons Library briefing paper (Aug 2020), The UK's contribution to the EU budget
[44] Commons Library briefing paper (Mar 2020), Brexit: the financial settlement – in detail
[45] See Office for Budget Responsibility (Oct 2018), Discussion paper No.3, Brexit and the OBR's forecasts, and Institute for Government (Oct 2018), Understanding the economic impact of Brexit

Most studies present their results in the form of GDP is x% different in a given scenario compared to the UK remaining in the EU. It is important to note that the UK economy would still grow in all Brexit scenarios considered, just at different speeds. The scenarios with slower *growth* results in the GDP *level* in the long term being lower than scenarios with higher growth.

The stylised diagram below provides a guide to interpreting such studies. In this example, the headline result of the study is that GDP is x% lower compared to the baseline.

Stylised example of how to interpret analysis of long-term GDP impact



All studies face the uncertainty that comes from the unprecedented economic event that Brexit is – in recent history, a developed economy the size of the UK has not left a large trading bloc such as the EU.

3.3 Economic studies: Deal and no-deal scenarios

As stated earlier, the vast majority of studies show UK GDP lower under both a deal and no-deal scenario, compared with the UK remaining in the EU. A no-deal outcome is associated with a greater hit to GDP in the long term.[46]

The Office for Budget Responsibility (OBR) bases its main economic forecasts on a selection of external economic studies, which it presented in the table below (FTA is Free Trade Agreement, a deal scenario; WTO represents a no-deal scenario).[47]

[46] See Office for Budget Responsibility (Oct 2018), Discussion paper No.3, Brexit and the OBR's forecasts, and Institute for Government (Oct 2018), Understanding the economic impact of Brexit
[47] OBR, Economic and fiscal outlook: November 2020, p.199, table B.1

Table B.1 Estimates of the long run effect on GDP of additional barriers on trade with the EU

	Per cent		
Organisation	FTA	WTO	Difference
Mayer et al (2018)	-2.4	-2.9	-0.5
Netherlands CPB (2016)	-3.4	-4.1	-0.7
UK in a Changing Europe (2019)	-2.5	-3.3	-0.8
Felbermayr et al (2018)	-1.8	-3.2	-1.4
Bank of England (2019)	-3.5	-5.0	-1.5
UK in a Changing Europe (2019)	-6.4	-8.1	-1.7
NIESR (2018)	-3.8	-5.5	-1.7
IMF (2018)	-2.0	-3.8	-1.8
Whitehall Study (2018)	-4.9	-7.6	-2.7
Netherlands CPB (2016)	-5.9	-8.7	-2.8
World Bank (2017)	-10.0	-13.0	-3.0
IMF (2018)	-3.3	-6.4	-3.1
OECD (2016)	-2.7	-7.7	-5.0
Average	**-4.0**	**-6.1**	**-2.1**

This shows the fairly wide range of estimates that are in the literature. They all, however, find the following two conclusions:

(i) a deal scenario results in a smaller economy in the long term than remaining in the EU single market and customs union;

(ii) a no-deal scenario would lead to a smaller economy in the long term compared with a deal scenario.

In its November 2020 forecasts for the UK economy, the **National Institute of Economic and Social Research** (NIESR) think tank estimated that UK-EU trade would be 46% lower by 2030 under a deal and 56% lower under a no-deal scenario, compared with staying in the EU. Foreign investment in the UK would also be lower.

NIESR estimates that GDP under a no-deal scenario would be 1.5% lower in the long run compared with a deal scenario.[48] NIESR previously estimated the impact of a deal scenario (a UK-EU free trade agreement) would result in UK GDP being around 4% lower in the long term.[49]

NIESR also observed that the adjustment from EU membership to a deal scenario is larger than the difference between deal and no-deal scenarios:

> While 'no deal' would represent a bigger adjustment for the UK economy than an FTA, with for example trade with the EU decreasing by a further 10 per cent, the majority of the adjustment would already have to happen even in the more favourable scenario of an FTA. While the possibility that the UK signs FTAs with other countries (like Japan) may support trade, we estimate that the mitigating effect would be very small compared to the direct cost of leaving the EU single market.[50]

3.4 Government analysis

In November 2018, the Government, led by then Prime Minister Theresa May, published analysis of the potential long-term impact of different

[48] NIESR, Prospects for the UK economy, 2 November 2020, F8
[49] NIESR, The Economic Effects of the Government's proposed Brexit Deal, November 2018
[50] NIESR, Prospects for the UK economy, 2 November, F12

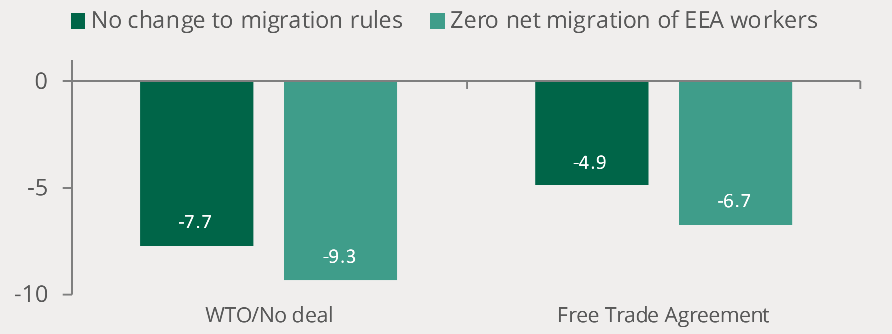
Brexit scenarios on the UK economy.[51] As of 18 December 2020, this is the last official economic analysis on the impact of Brexit published by the Government.

The analysis used economic models to compare how big the economy would be (measured by GDP) in different future UK-EU trading scenarios relative to a 'baseline' scenario of the UK staying in the EU.

The 2018 government analysis estimated that a deal – or free trade agreement – scenario with the EU would see GDP between 4.9% and 6.7% lower in 15 years compared with staying in the EU, depending on immigration policy. Under a 'no deal' scenario, GDP would be between 7.7% and 9.3% lower.[52]

UK long-term GDP impacts of Brexit (2018 Govt analysis)

% difference in GDP level in 15 years compared to staying in EU



[Source: HM Govt, EU Exit: Long-term economic analysis, Nov 2018]

Some criticised the analysis for some of the assumptions made and arguably under-estimating the potential benefits from new free trade deals with non-EU economies.[53]

The Treasury's Permanent Secretary downplayed the relevance of the November 2018 government analysis in a recent Treasury Committee evidence session:

> That analysis is now two years old. It was prepared for a previous Government and it was also prepared under assumptions set by that Government […]
>
> First of all, we have not updated that assessment. Secondly, the assessment at the time was about a no-deal Brexit. Obviously, we have passed that point. We left the EU at the end of January with an agreement. […] The third thing to say is that the effect of the pandemic on our economy, the European economy and every other economy has considerably changed the picture. […]
>
> Two years ago when people were talking about no deal they meant literally leaving with no agreement at all. That did not happen. We left with a withdrawal agreement. You are of course

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[51] HM Government, EU Exit: Long-term economic analysis and EU Exit: Long-Term Economic Analysis Technical Reference Paper, November 2018

[52] This no-deal scenario was based on no Withdrawal Agreement (which has subsequently been agreed) and no future trade deal

[53] See for example, Julian Jessop, Will a vote for the Johnson deal boost the British economy?, CapX, 18 October 2019 and Treasury Committee report, The UK's economic relationship with the EU: The Government's and Bank of England's Withdrawal Agreement analyses, HC 1819, December 2018

> right that there is a big question about the future agreement. That is different from what was understood at the time to be no deal.[54]

A summary of the report's analysis is provided in the Library briefing paper Brexit deal: Economic analyses (December 2018) and the Library Insight Brexit deal: Potential economic impact (October 2019) written shortly after the Withdrawal Agreement was negotiated between the UK and EU.

4. Further information

Additional reading:

- Commons Library, End of Brexit transition period: Deal and no-deal scenarios, the hub for Library briefings on this topic
- Commons Library briefing paper (Dec 2020), End of Brexit transition: trade
- Commons Library briefing paper (Dec 2018), Brexit deal: Economic analyses
- Bank of England, Monetary Policy Report: November 2020
- Office for Budget Responsibility, Economic and fiscal outlook: November 2020, Annex B: Brexit scenarios
- Institute for Fiscal Studies (Oct 2020), Green Budget: chapter 3 'The cost of adjustment: emerging challenges for the UK economy' (authored by Citi)
- UK in a Changing Europe (Sep 2020), What would no deal mean
- HM Government (Nov 2018), EU Exit: Long-term economic analysis and EU Exit: Long-Term Economic Analysis Technical Reference Paper
- Office for Budget Responsibility (Oct 2018), Discussion paper No.3, Brexit and the OBR's forecasts
- Institute for Government (Oct 2018), Understanding the economic impact of Brexit

[54] Sir Tom Scholar, Permanent Secretary HM Treasury, Oral Evidence to Treasury Committee, 11 November 2020, Q108-112

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