

## “Brexit and the future of global trade”

London, 3<sup>rd</sup> July 2017

### CONFERENCE REPORT

#### Introduction

In the latest of its series of seminars on aspects of Brexit, The Federal Trust, the Global Policy Institute, and the Konrad Adenauer Stiftung brought together a panel of three experts to discuss some of the more significant implications for the UK’s global trade position following the Brexit vote in 2016. **Dr Rebecca Harding**, Founder and CEO of Equant Analytics and a former Chief Economist of the British Banking Association was joined by **Dr Gunnar Pohl**, a tax expert and the Deputy Director of the German-British Chamber of Industry and Commerce and **Catherine Stewart**, a Public Affairs expert and partner of Jericho Chambers.

Introducing the seminar, the Director of the Konrad Adenauer Stiftung’s London Office, **Hans-Hartwig Blomeier** noted that even though more than a year had passed since the Brexit Referendum vote, and more than three months had passed since the triggering of Article 50, there had been little movement or indeed progress on the UK formulating any coherent position. One brief meeting in Brussels seemed a very modest milestone for such a momentous itinerary.

**Professor Stephen Haseler**, Director of the Global Policy Institute observed that the Brexiteers’ thesis that the UK would be able to “walk tall” immediately in a post-Brexit world would be tested to destruction in the event of negotiations failing to secure a transition period.

Finally **Brendan Donnelly**, Director of The Federal Trust said that even if Brexiteers believed there was no place for experts in this debate, the present seminar would benefit from the presence of three experts who were both knowledgeable and eloquent.

In the event, all three experts left the audience in no doubt that the consequences of Brexit for the UK in terms of global trade were going to be considerable with much of the burden falling on small to medium sized businesses, especially in the manufacturing sector.

#### Panel Discussion

##### **Dr Rebecca Harding**

Drawing on recent research for her latest book, Dr Harding gave a stark analysis of the “seismic shift” which she believed had occurred in global trading patterns during the last few years. A reaction against global free trade had been noticeable for some time. Even before the election of Donald Trump and the Brexit vote in the UK, trade was becoming increasingly used as a tool of foreign policy. The language of trade was being “weaponised”, she said. Moreover, this seismic shift away from globalisation had been

accompanied by another shift no less dramatic, namely a sharp drop in global trade growth in the G20. As recently as 2011 the WTO had been forecasting an 11 % growth in average global trade growth, or at the very least two and half times GDP. Current global trade growth however was a desultory 0.8% of GDP. This loss of momentum in global trade was partly a symptom of politics increasingly taking over from economics in trade considerations.

Recent projections for UK global trade were expecting sharp falls in UK trade with Asia and the US. Only trade with the EU, ahead of Brexit, had been predicted to rise. Of the top 12 sectors of UK Trade, these five: Electronics, Aerospace, Pharmaceuticals, Oil and Machinery, dominated over 60% of current trade patterns between the UK and the EU. Of these, 29% of UK exports to the EU were of goods known as “Dual Use” (i.e. capable of being used for military as well as civilian purposes.) Significantly, all UK exports had a strong correlation (73%) to the value of the euro and no or little correlation to the value of sterling. Thus Brexit threatened to exacerbate the negative effects for the UK of already existing shifts away from globalization towards economic nationalism.

Meanwhile, the US under Trump was demonstrating that economic nationalism could even outweigh some domestic political arguments. Thus the controversial decision to build a wall to prevent Mexicans entering the US, a policy move which had played a central role in Trump’s election campaign, had been quietly shelved after protests from Texan oil companies keen not to lose lucrative refinery markets in Mexico.

In such an atmosphere of rising trade nationalism even the EU was not immune from sentiments “weaponising” trade and this could impose significant burdens on the UK post Brexit. Concluding her presentation, Dr Harding feared that without greater cooperation and humility the “weaponisation” of trade would continue apace.

### **Catherine Stewart**

Ms Stewart’s presentation attempted to quantify the effects on the UK economy of Brexit were it carried out in the form currently proposed by the government. Brexit as currently proposed by the UK government envisages a complete break with the Single Market and the Customs Union. The UK was therefore risking losing all the significant benefits of the Single Market. These included streamlined infrastructure, liberalised airlines, smooth running car-supply chains, possibilities for the greater specialization of companies, administrative simplification and harmonization and an overall reduction of bureaucracy as well as the trading benefits of a wider market.

As Ms Stewart recalled, during the distant days of the pre-Single Market European Union, delays at frontiers quickly translated into increased costs for business. The thought of returning to an era of long queues for UK lorries could not be a welcome prospect for any business presently located in the UK dependent on EU supply chains.

As an example of the manifold benefits of the present EU system, Ms Stewart referred to London’s “Silicon Valley”, the technology hub around Shoreditch and Old Street in the City of London, a perfect example of the new “gig economy” where neither nationality nor bureaucracy impacted the entrepreneurial process. More than 35,000 EU citizens had set up businesses in the UK, taking advantage of these conditions which enabled them seamlessly to do business with the rest of the EU. This hub was not expected to remain long in London post-Brexit.

Ms Stewart predicted that many small businesses would be weakened by the increased administrative costs arising from Brexit. Larger businesses would be able to cope better

with these costs but they would have to relocate their critical functions to other parts of the EU. There would be a loss of skills in the UK as highly trained specialists moved back to the EU. Entirely new institutions would have to be created to replicate EU structures such as trade inspectorates. All the uncertainty surrounding these developments was causing not only “Brexiety” but also “Brexodus”.

Many of those leaving were highly skilled and could afford to move abroad. They were also often major contributors to the UK economy and tax system. The liquidation of real estate and sterling assets as they moved was already having an impact on sectors of London’s economy.

The election of Macron in France and his determination to liberalise the French economy would, if successful, almost certainly lure significant numbers of the 800, 000 French citizens currently working in the UK back to Paris and other French cities. Many of these French businesses had benefited from the UK’s liberalised economy and would be well placed to impart considerable commercial experience to a reforming France eager to learn and embrace the best of Anglo-Saxon capitalism.

These concerns and developments had still not been factored in by many British businesses. In a recent survey only 30% of businesses had changed their strategy to cope with Brexit. More than 50% polled said they had no idea what WTO trading rules would mean for their businesses. 30% said they had imposed a hiring freeze.

Companies were being told by the government to be “positive” about Brexit but companies were finding this difficult. Many were, recognizing that trying to strike trade deals with countries outside the EU can be difficult. Where countries such as China, Japan or India have the opportunity to strike deals with the EU as a whole, it would be highly unlikely that any deal with the UK as a stand-alone entity would be more advantageous. In fact as recent attempts to strike a deal in India had proved, the UK negotiating hand was weak and incoherent, incapable of negotiating deals without having to grant concessions on such areas as immigration which would be domestically unacceptable.

As Lord Patten had recently observed, businesses could be forgiven for “not knowing quite what was happening” because the government itself did not have the “faintest idea” of what was happening.

Imminent attempts by the Brexit Secretary David Davis to “sit down with business” were unlikely, in Ms Stewart’s view, to dispel the widespread misconception of the reality of Brexit’s consequences for UK business.

Summing up Ms Stewart noted that businesses needed “the oxygen of confidence” to make plans.

### **Dr Gunnar Pohl**

Dr Pohl evaluated the effects of Brexit on the German-British trading relationship. He noted the fundamental asymmetry of the relationship with annual UK imports of German goods (90 billion euros) far exceeding German imports of UK goods (38 billion euros). Only 8% of Germany’s global exports went to the UK and, despite many UK media reports to the contrary, the loss of UK markets was unlikely to have a decisive effect on the German economy. Nevertheless, in certain sectors such as automotive parts there was a strong interdependency which made the sector as currently structured an effective two-way system. In this context, Dr Pohl noted that UK consumers had benefited from this and while they had been critical of EU regulations they had yet to demonstrate that this criticism spilt over into their appreciation of EU products and goods.

Despite the uncertainty arising from the Brexit vote, current projections for trade in goods did not point to any significant impact for 2018. Thereafter, however, there was less certainty. Dr Pohl drew the audience's attention to the importance of the *Mittelstand* in Germany and its role as the traditional backbone of German industry. These companies were highly risk-averse and cautious. They were unlikely to view the uncertainty in a positive light and would therefore almost certainly freeze their investment plans in the UK.

Given the fear that right-wing parties might exploit these tensions, German business on the whole had been reticent in voicing its concerns publicly. These concerns were not only related to investment, manufacture and exports but also included the issue of the free movement of labour which had benefited several sectors of both countries' economies, notably construction.

The results of Brexit however were most likely to impact the UK significantly more than Germany. The UK almost certainly will have to pay a higher cost for its service sector and generally the higher costs of Brexit would be borne by the UK in Dr Pohl's opinion.

Echoing the views of most continental analysts, he believed that a "soft Brexit" might be more likely following the General Election even though several members of the panel questioned whether a so-called "soft Brexit" was an intellectually sustainable concept.

Turning to the financial services sector, Dr Pohl referenced the decision of Goldman Sachs to double the number of bankers they currently employ in Frankfurt. Japanese banks such as Nomura were also relocating to Frankfurt and Dr Pohl expected this trend to continue. In Dr Pohl's view Germany would "cope fairly well" with the impact of Brexit.

Dr Pohl ended on a positive note: the UK business community, he noted, appeared to be becoming more aware of the consequences of Brexit. Moreover, it would be important for the EU to recognize that the UK had always been a net contributor to the EU and that Europe post-Brexit would speak with more than one voice. To avoid the danger of Europe becoming less influential post-Brexit, it was important that the EU chose a more "generous option" with regard to the UK.

## Discussion

In a lively discussion with many interesting contributions from the floor, the panel sought to explain what the "most visible effects" of Brexit were likely to be and whether the UK position post the election had shifted. The first questions reflected these issues.

**Dr Harding** characterized the effects of the recent election in the following way: "Although there has not been a shift in the government's thinking there has been a material shift of the context in which negotiations are conducted". The overriding importance of the five strategic sectors of UK trade implied the need for humility as it was difficult to imagine how complicated supply chains could function without a pan-European framework.

Several questions reflected the interest in the post-Brexit agriculture sector, including dairy products, but Dr Harding noted that although this was an important part of the equation, in economic terms the Fisheries/Agriculture sector was not on a scale comparable to the "big five sectors".

**Catherine Stewart** warned that Welsh lamb would come under considerable threat should the UK conclude a deal with New Zealand. It was noted from the floor that Welsh agricultural matters would under present devolution arrangements be an issue for Wales rather than Westminster. Ms Stewart also emphasized that there was much talk of

“access” to the Single Market, but access was always based on compliance with the rules of the Single Market over which the UK post-Brexit would have no control.

**Dr Pohl** strove to distinguish between goods of basic and more complex origin. He noted that Lidl, the well-known German supermarket, sourced much of its food locally. Goods of more complexity not sourced locally were likely to be more impacted by Brexit and the price of such goods would rise.

**Dr Harding** drew the audience’s attention to the dependency of much UK manufacturing on “Just in time delivery”. She predicted that this sector would find it hard to survive any delays imposed by Brexit. It was essential in her view for manufacturing that the UK remains in the EEA or at least Part II of the EEA agreement.

**Professor Vernon Bogdanor** asked from the floor whether an unprotected market might be a gain post-Brexit. Were there ever increasing benefits to be had from Free Trade, asked another member of the audience? Why did the Conservative Party reject trading advantages of the Single Market? **Brendan Donnelly** reminded the audience that one of the aspects of the larger paradoxes of Brexit was that the Conservative party was in theory *par excellence* traditionally the party of Free Trade but was now advocating leaving the free trading European Union.

### Conclusions


**Dr Harding** believed that the disruption of supply chains would directly affect the productivity of the UK. The UK already had a productivity problem and this would exacerbate problems with trade finance. There was a lack of democratic legitimacy in the process of globalisation. **Professor Haseler** supported this argument, emphasizing the huge inequalities which globalization had caused.

**Ms Stewart** concluded that it was very difficult to imagine how businesses could reorientate themselves without more support and guidance from the government, particularly with regard to which markets they should be seeking to find deals.

**Brendan Donnelly** noted that there was much confusion in the UK about globalisation and the EU. It was the role of governments to mitigate the effects of globalisation and ensure that the fruits of globalisation were more equitably distributed. It had been one of the more intellectually indefensible aspects of the Brexit narrative that somehow the EU was to blame for this inequitable distribution implemented by years of Conservative governments.

**Dr Pohl** observed that any customs controls were a disaster for companies having to deal with “Just in time” issues. A member of the audience observed that Germany was making huge strides in Artificial Intelligence and robotic mechanization. There were 178 robots in Germany for every 10,000 employees compared to only 33 robots for the same number of employees in the UK. He posed the question; “Is the certainty of Brexit any less damaging than uncertainty?”

Summing up, **Brendan Donnelly** observed that Dr Harding’s call for humility was well-placed but that Brexit had been an act of “arrogant, childish irrationality” and to expect it to be implemented with humility, maturity and rationality was wholly unrealistic. There were no congenial choices available for the UK and the entire “ramshackle intellectual edifice” on which Brexit was constructed boiled down to a policy of “Have Your Cake and Eat it”. It was unfair to criticize only Boris Johnson for saying this when the entire political class in favour of Brexit had believed it.



Unlike the EU which had played its opening rounds with an open hand, the UK could not afford to reveal its cards “because it simply does not have any”. The objective of having a cake and eating it in this context was unsustainable and the chances of the UK walking out of the first phase of talks were high given that the second phase of talks on trade would expose the UK’s weakness for all to see.

Richard Bassett  
10<sup>th</sup> July 2017