Durham University
Centre for Banking, Institutions and Development

CBID Briefing Note 2213

Analysis of the UK Government's 'No-Deal' Tariff Schedule

Anamaria Nicolae and Michael Nower
March 2019

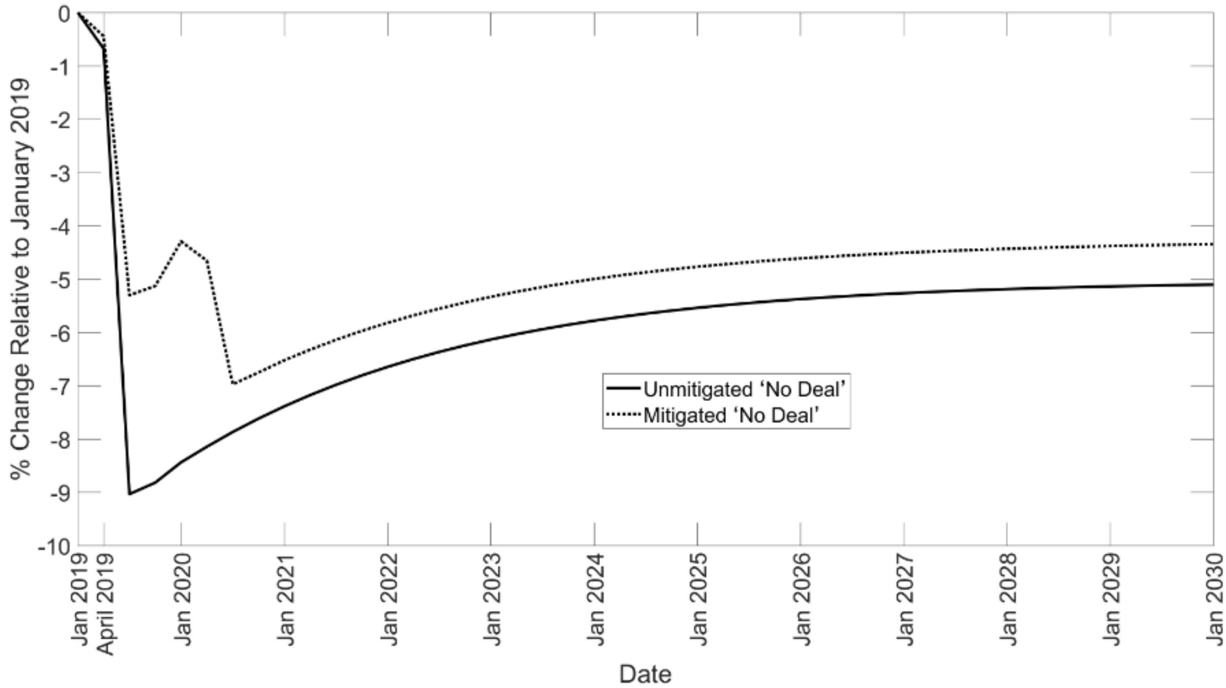
OVERVIEW:

This briefing note quantifies the short term impact of the UK Government's 'No-Deal' Tariff Schedule on UK GDP in the event of a 'No-Deal' Brexit.

On March 13th 2019, the UK Government announced its Temporary rates of custom duty (tariffs) on import in the event of a 'No-Deal' Brexit. Under this tariff schedule, tariffs will be set to 0% on most UK imports from the date of the UK's exit from the EU (currently 29th March 2019) for 12 months, until the 29th of March 2020. After this point, the UK is currently set to apply the EU's current World Trade Organisation (WTO) Most Favoured Nation (MFN) tariff schedule. In addition to the temporary tariff schedule, the UK has also agreed to continue the application of (grandfather) existing EU agreements with the following countries/regions: the EEA countries, Switzerland, Liechtenstein, Chile, Eastern and Southern African States, Faroe Island, Israel and the Palestinian Authority.

This briefing note considers the short and long term impact of the UK Government's 'No-Deal' Tariff Schedule and grandfathered agreements on the expected path of UK GDP in the event of a 'No-Deal' Brexit, using a bespoke macroeconomic model of international trade developed at Durham University. (See CBID Policy Note 2712 for more details on the macroeconomic model).

SIMULATED UK GDP:



The chart above presents the simulated path of UK GDP under two scenarios: an unmitigated 'No-Deal' where the UK leaves the EU on full WTO terms with no agreements grandfathered, and applies the EU's MFN tariffs on all imports (the solid line), and a mitigated 'No-Deal' where the UK grandfathers the agreements listed above and applies the announced 'No-Deal' Tariff schedule until March 2020, after which it applies the EU's MFN tariffs on all imports (the dotted line). In the second scenario, we also assume that the UK is able to grandfather the other EU agreements over the period covered by the 'No-Deal' tariff schedule, and that these also come into force in March 2020.

As the chart shows, although the government's 'No-Deal' tariff schedule, and the announced grandfathered agreements dampen the impact of a 'No-Deal' Brexit, UK GDP is still expected to fall significantly in the short-run (approximately 5.3%), and once the long-term tariff schedule is applied UK GDP is expected to fall further. The falls in UK GDP remain large for two reasons: first, because UK imports will still face large increases in non-tariff barriers, such as customs checks in the event of a 'No-Deal' Brexit, and second, because the UK's 'No-Deal' tariff schedule does nothing to protect UK exporters to the EU, who will face full EU WTO MFN tariffs, and will therefore see significant profits decreases, which will have knock on effects on the real wages and employment of the workers in the exporting firms. However, even with these remaining negative effects the fall in UK GDP is much lower than in an unmitigated 'No–Deal', where the short-run drop in UK GDP could be as large as 9%.

It is worth noting that future UK Free Trade Agreements with countries the EU does not currently have existing agreements, such as the USA, Australia, New Zealand, India and China could significantly change the expected long-run path of UK GDP (post-2021). However, such FTAs can have no effect on the short-run behaviour of GDP - and thus a 'No-Deal' Brexit is still likely to be extremely disruptive in the short-run. One possible way to dampen the sharp fall in the short run would be to increase the period of time over which the 'No-Deal' tariff schedule is in place, although this will come at the expense of increased competition for UK domestic producers.