Written Evidence to the House of Commons International Trade Committee
in relation to its inquiry “The COVID-19 pandemic and international trade”

Executive Summary

1. Publicly available UK economic forecasts and surveys are clearly indicating both a very sharp negative economic impact of the COVID-19 crisis during 2020 and longer-term unemployment challenges, as well as a very substantial decline in trade between the UK and third countries.

2. Most medium- and long-term impacts will be dependent on the severity of the economic crisis to follow the pandemic, both in the UK and abroad. However, there should be little doubt that supply chains will be severely disrupted, at least in the medium-term, and in particular if any relevant trading country needs to enter a second or ulterior period of lockdown.

3. Given its close trade ties, the UK is particularly exposed to the continuity of its trade with the European Union (EU), which has last been estimated to represent 45% of all UK exports and 53% of all UK imports. The intensity of these trade ties is likely to mean that, given a breakdown of existing supply chains, alternative arrangements available to UK businesses are likely to remain significantly concentrated in the EU and, likewise, UK businesses could take the position of bankrupt or temporarily unavailable suppliers in EU businesses’ supply chains.

4. Under the current circumstances, the added uncertainty surrounding the on-going negotiations of a future UK-EU trade relationship can only compound the likely negative impact of the COVID-19 pandemic for UK businesses trading internationally and for the UK’s public sector in the medium- and long-term. The uncertainty surrounding the continuity of existing and new supply chain arrangements between the UK and the EU once the transition period ends can have severe chilling effects on UK businesses trading internationally and EU businesses supplying the UK.

5. Any material change to the trading terms between the UK and the EU is bound to have a very large negative impact for the UK economy. Before Brexit, the UK Government had assessed it at a loss of between 6.7 and 9.3% in GDP level in 15 years compared to staying in the EU. Under the current circumstances, the negative economic impact could be even larger.

6. **The single most effective intervention at this stage would be for the Department for International Trade to lead on the negotiations with the EU for a two-year extension of the transition period** under Article 132 of the Agreement on the withdrawal of the United Kingdom from the European Union and the European Atomic Energy Community. Concerns about the UK’s contribution to the EU budget as a result of an extension of the transition period are unwarranted.

7. Postponing the end of the transition period to 31 December 2022 would create the necessary space not only for the future UK-EU trade relationship to be properly negotiated, but also to avoid adding the pressure of no-deal contingency planning to the already extreme circumstances under which UK businesses trading internationally and the parts of the UK public sector that rely on trading with international suppliers and contractors, are expected to operate post COVID-19.

Submission

This document addresses some of the questions formulated by the UK Parliament’s International Trade Committee in its inquiry “The COVID-19 pandemic and international trade” and, in particular:

- **What medium- and long-term negative impacts could arise from the pandemic for UK businesses trading internationally? What steps could the Government take to mitigate these impacts?**
How should the Department for International Trade work with the rest of central government, as well as devolved, local and regional government, to deliver a coordinated response to the pandemic?

How can the UK Government engage with countries at the World Trade Organization and bilateral trading partners – including those with which the UK has a significant trading relationship or one facilitating trade in priority goods – to promote international cooperation and a coordinated global response to the pandemic?

In short, the document stresses that the extremely likely negative impact of the COVID-19 pandemic for UK businesses trading internationally and for the parts of the UK’s public sector that rely on trading with international suppliers and contractors in the medium- and long-term can only be compounded by the uncertainty surrounding the on-going negotiations of a future UK-EU trade relationship. The single most effective intervention at this stage would be for the Department for International Trade to lead on the negotiations with the EU for a two-year extension of the transition period in conformity with Article 132 of the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community.¹

1. Background

a) Forecasting with any precision the medium- and long-term effects of the COVID-19 pandemic on UK businesses trading internationally, and on the parts of the UK public sector that rely on trading with international suppliers and contractors, is extremely difficult under the current uncertainty. However, publicly available estimates are clearly indicating both a very sharp negative economic impact during 2020 and longer-term unemployment challenges.² Publicly available surveys also show a very substantial decline in trade between the UK and third countries—with 57% of importers and 59% of exporters reporting that trade has been affected by COVID-19 in March 2020,³ thus aggravating early signs reporting that both total and export order books worsened considerably in February 2020.⁴

b) Most medium- and long-term impacts will be dependent on the severity of the economic crisis to follow the pandemic, both in the UK and abroad. However, there should be little doubt that supply chains will be severely disrupted, at least in the medium-term, and in particular if any relevant trading country needs to enter a second or ulterior period of lockdown. In that regard, the World Trade Organisation (WTO) has forecasted that ‘World merchandise trade is set to plummet by between 13 and 32% in 2020 due to the COVID-19 pandemic’, where ‘Nearly all regions will suffer double-digit declines in trade volumes in 2020, with exports from North America and Asia hit hardest’. It also stressed that ‘A 2021 recovery in trade is expected, but dependent on the duration of the outbreak and the effectiveness of the policy responses.’⁵

Note: all websites last visited on 21 April 2020.


April 2020
2. The UK’s economic exposure to the European internal market, pre- and post- COVID-19 crisis

a) Given its close trade ties, the UK business sector is particularly exposed to the continuity of its trade with the European Union (EU), which has last been estimated to represent 45% of all UK exports and 53% of all UK imports.\(^6\) Remarkably, this bilateral trade dependence between the UK and the EU does not only affect UK businesses, but also significant parts of the public sector that rely on trading with international suppliers and contractors, which I have previously estimated at 15% of the total value of all UK public procurement, affecting a wide range of sectors.\(^7\)

b) The intensity of these trade ties between the UK and the EU is likely to mean that, given a breakdown of existing supply chains, alternative arrangements available to UK businesses are likely to remain significantly concentrated in the EU and, likewise, UK businesses could take the position of bankrupt or temporarily unavailable suppliers in EU businesses’ supply chains. The likely continuity of this bilateral trade dependence is plausible, not least because alternatives in other main economic regions are forecasted to be particularly impacted by the COVID-19 crisis. As above, the WTO has stressed that ‘exports from North America and Asia [will be] hit hardest’ during 2020, which will limit the availability of opportunities in those areas for UK businesses and UK public sector procurers.

3. Additional Brexit-related uncertainty

a) Under the current circumstances, the added uncertainty surrounding the on-going negotiations of a future UK-EU trade relationship can only compound the likely negative impact of the COVID-19 pandemic for UK businesses trading internationally and for the UK’s public sector in the medium- and long-term. It is publicly notorious that UK-EU negotiations have been significantly delayed by the COVID-19 crisis,\(^8\) and that the current timetable is extremely unlikely to deliver a positive, comprehensive framework for a UK-EU future trade relationship—given that there were concerns as to the feasibility of such a goal even under the originally unaffected 11-month timetable.\(^9\) Indeed, even before COVID-19, a no deal cliff-edge at the end of 2020 was seen as the most likely scenario by a number of experts.\(^10\)

b) The uncertainty surrounding the continuity of existing and new supply chain arrangements between the UK and the EU beyond 31 December 2020, once the transition period ends, can have severe chilling effects on UK businesses trading internationally. UK businesses will not be able to assess whether any efforts and additional investments to reorganise their supply chains or look for export opportunities to the EU will continue to generate results from 1 January 2021. UK businesses will find themselves in the very difficult position of having to

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manage the long tail effects of the COVID-19 pandemic while also keeping in place or boosting their no-deal preparations. This will force them to spread their resources rather thinly or, most likely, to make difficult decisions on the contraction or interruption of their business activities with the EU. Likewise, EU businesses trading with the UK will have to make similar decisions and this could deprioritise investments aimed at maintaining or establishing new supply chain relationships with UK businesses and customers. This is reflected in recent business surveys, which not only show that Brexit-related business uncertainty remains high and at 2018 levels (after even higher levels during 2019), but also that COVID-19 related uncertainty is generating a significant pressure on businesses to the point of leading 71% of them to forecast negative impacts of COVID-19 on their level of activity over the next year.\footnote{N Bloom, P Bunn, S Chen, P Mizen and P, 'The economic impact of coronavirus on UK businesses: Early evidence from the Decision Maker Panel' (VoxEU.org, 27 March 2020) \url{https://voxeu.org/article/economic-impact-coronavirus-uk-businesses}.}

\subsection{c) None of this is conducive to economic recovery, let alone growth in the UK. The continued existence of a ‘no deal’ threat weighs down the UK’s economic prospects. Any material change to UK-EU trading terms is bound to have a very large negative impact for the UK economy. Before Brexit, the UK Government had assessed it at a loss of between 6.7 and 9.3% in GDP level in 15 years compared to staying in the EU.\footnote{D Harari, Brexit deal: Potential economic impact (House of Commons Library blog, 18 October 2019) \url{https://commonslibrary.parliament.uk/brexit/brexit-deal-potential-economic-impact/}.} Under the current circumstances, the negative economic impact could be even larger. And it could have further knock-on effects if the combined effect of Brexit and the post- COVID-19 economic crisis result in a factioning of the UK’s internal market.\footnote{See eg J Duffy, ‘Coronavirus and Brexit double will mean economic “Stone Age”’ (National, 12 April 2020) \url{https://www.thenational.scot/news/18374765.brexit-covid-19-double-will-mean-economic-stone-age/}.}

\section{4. Final remarks}

\subsection{a) In view of all the above, the single most effective intervention at this stage would be for the Department for International Trade to lead on the negotiations for a two-year extension of the transition period under Article 132 of the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community.\footnote{A similar view has been expressed by C Tindall, ‘A Brexit extension will help stop this crisis becoming a disaster’ (LSE Brexit blog, 20 March 2020) \url{https://blogs.lse.ac.uk/brexit/2020/03/20/a-brexit-extension-will-help-stop-this-crisis-becoming-a-disaster/}.}}

\subsection{b) Concerns about the UK’s contribution to the EU budget as a result of an extension of the transition period are unwarranted.\footnote{For reports, see eg ‘Why the government will not ask for a Brexit extension’ (Economist, 18 April 2020) \url{https://www.economist.com/britain/2020/04/18/why-the-government-will-not-ask-for-a-brexit-extension}.} The UK’s contribution to the EU budget in case of an extension needs to be negotiated and agreed by both parties in the context of the Joint Committee. Presumably, the UK’s contribution would be commensurate to the benefits of the extension to the UK and its participation in EU programmes to mitigate the impact of COVID-19 across the EU economy. A rejection by the UK Government to seek a negotiated extension on the assumption that it would be making a net contribution (that is, funding more than it benefits from the extension) ignores that the contribution needs to be agreed by the UK and, perhaps, presumes a weak negotiating position on the UK’s side.

\subsection{c) Postponing the end of the transition period to 31 December 2022 would create the necessary space not only for the future UK-EU trade relationship to be properly negotiated,
but also to avoid adding the pressure of no-deal contingency planning to the already extreme circumstances under which UK businesses trading internationally and the parts of the UK public sector that rely on trading with international suppliers and contractors, are expected to operate post COVID-19.