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# **IMPACT OF BREXIT ON INTERNATIONAL TRADE**

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Brexit refers to the official separation of the United Kingdom from the European Union (EU), which took place on January 31, 2020. The phrase Brexit is a mnemonic device created to represent the departure of the United Kingdom. During a referendum conducted on June 23, 2016, almost 52 percent of the British voters who took part expressed their preference to withdraw from the European Union, so establishing the precedent for the United Kingdom to become the first nation to do so. The negotiations pertaining to the separation process spanned over a period of more than two years subsequent to the formal submission of Britain's request to exit in March 2017. In the end, the achievement of Brexit was realised under the tenure of Boris Johnson the successor of Theresa May.

In June 2022, Johnson tried to abrogate a portion of the trade agreement by proposing legislation in Parliament that would eliminate restrictions on the importation of products into Northern Ireland from other regions within the United Kingdom. The Johnson administration claimed that the EU's excessively strict implementation of customs regulations was eroding commerce and jeopardising peace in Northern Ireland. Unionists expressed concerns over the potential negative impact of customs checks on Northern Ireland's diplomatic ties with the United Kingdom. Consequently, the Democratic Union Party (DUP) declined to re-enter Northern Ireland's power-sharing executive unless the removal of these inspections was ensured. Critics of Johnson's decision, such as May, contended that the action was in violation of the law, and the European Union issued a warning of potential reprisals.

The Brexit has had a lasting economic effect on International Trade within and outside Europe. Within this paper, we will explore the different ways in which international trade has been affected.

## **INTRODUCTION**

Brexit was the withdrawal of the United Kingdom (UK) from the European Union (EU). The formal occurrence of Brexit took occurred at 23:00 GMT on 31 January 2020 (00:00 1 February 2020 CET) after to a referendum held on 23 June 2016. The UK is the sole independent nation that has withdrawn from the European Union. Since 1 January 1973, the United Kingdom has maintained its membership in the European Union (EU) or its precursor, the European Communities (EC). After the occurrence of Brexit, the supremacy of EU law and the Court of Justice of the European Union over British legislation has been revoked. The European Union (Withdrawal) Act 2018 preserves pertinent European Union legislation as domestic legislation, allowing the United Kingdom to modify or revoke it. The European Union (EU) and its institutions had a slow development subsequent to their foundation. Eurosceptic factions have been present over the duration of British membership, expressing opposition towards various components of the European Union (EU) and its predecessors.

## **TRANSITIONAL PERIOD CUSTOMS & TRADE**

### **AGREEMENTS**

David Frost and Michel Barnier persisted in their efforts to negotiate an enduring trade agreement throughout the transition period. A agreement was mutually declared reached by both parties on December 24, 2020. On December 30, both chambers of the British parliament approved the agreement, which was subsequently granted Royal Assent in the wee hours of the following day. The transition period came to a close the evening after, in accordance with its provisions. The European Parliament delayed setting a date to ratify the agreement after the United Kingdom announced it would unilaterally extend a grace period precluding trade checks between Northern Ireland and the United Kingdom. Later, on April 27, a vote was subsequently scheduled, and the measure was approved by an overwhelming majority.<sup>1</sup>

A temporary customs agreement was in effect until 1 July 2021. Traders who imported standard products from the EU to the UK during this period had the option to postpone the submission of their customs declarations and payment of import taxes to HMRC for a maximum of six months. This arrangement was implemented with the intention of streamlining and circumventing import

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<sup>1</sup> Zimmermann, Hubert. "Brexit and the External Trade Policy of the EU." 6 *European Review of International Studies* 29 (2019)

constraints in the initial stages of the new circumstances. Its purpose was to streamline inbound trade amidst the COVID-19 pandemic and mitigate significant disruptions in domestic supply chains in the immediate term.<sup>2</sup> In response to concerns of unprepared border infrastructure, the UK government has extended the deadline for import inspections from the EU to the UK until the end of the year. This decision was made to prevent any disruptions in the supply chain during the current Covid problem. Subsequently, there was another postponement of import controls due to a scarcity of truck drivers. The implementation of these measures is planned to occur gradually during 2022.

## **EFFECT OF THE BRITISH EXIT FROM THE EUROPEAN UNION**

### **Trade Relations Between the United Kingdom and the European Union**

“Before Brexit, the United Kingdom enjoyed a significant level of economic integration with the European Union, which resulted in the advantages of the single market and the customs union. Following Brexit, the United Kingdom withdrew from the single market and customs union, leading to alterations in the trade dynamics.”<sup>3</sup>

In the year 2020, the European Union (EU) constituted around 43% of the United Kingdom's overall exports. Conversely, the United Kingdom emerged as the EU's third-largest trade partner, contributing approximately 9% to the EU's total exports. The presented data demonstrates the notable level of economic interdependence between the two institutions.

### **Trade Barriers & Tariffs**

Brexit has led to the emergence of trade obstacles and tariffs between the UK and the EU. Although a trade deal, referred to as the Trade and Cooperation deal, has been established between the United Kingdom and the European Union, it is evident that commerce between these two institutions is no longer devoid of obstacles.<sup>4</sup>

Following the UK's withdrawal from the EU's single market and customs union, customs procedures, border inspections, and regulatory requirements have been reinstated. These modifications have augmented administrative encumbrances and expenses for enterprises

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<sup>2</sup> Ibid

<sup>3</sup> bancaitalia.it

<sup>4</sup> Nicola McEwen, David Eiser, Graeme Roy, et.al., “The Trade Policies of Brexit Britain: The Influence of and Impacts on the Devolved Nations” 1 European Review of International Studies 25 (2021).”

involved in UK-EU commerce.

### **Disruptions in the supply chain**

The occurrence of Brexit has resulted in significant disruptions to supply chains, specifically impacting companies that heavily depend on just-in-time manufacturing and cross-border transportation. The heightened border inspections and regulatory mandates have resulted in disruptions to the flow of commodities and introduced intricacies to the management of supply chains.

### **Services Trade**

Effects on Services Brexit has had an impact on services trade, including several industries such as banking, professional services, and digital services. The Trade and Cooperation Agreement include restrictions pertaining to restricted market entry in services; nevertheless, it does not offer an equivalent degree of access as the United Kingdom had during its membership in the single market.<sup>5</sup>

UK service companies operating in the EU are currently encountering difficulties due to the introduction of additional regulatory obstacles and limitations on their ability to enter the market. Likewise, European Union service companies encounter obstacles when attempting to enter the UK market.

### **The potential for international trade**

The occurrence of Brexit has presented the UK with prospects to establish fresh trade alliances outside of the European Union. The United Kingdom, as an autonomous trading nation, possesses the capacity to engage in negotiations for trade agreements with nations that are not part of the European Union.<sup>6</sup> The United Kingdom has already entered into trade agreements with many nations, such as Japan and Canada.

The primary objective of these recently established trade agreements is to augment market accessibility, diminish trade impediments, and foster economic collaboration. Nonetheless, it will require a considerable amount of time to evaluate their whole influence on the United Kingdom's global trading environment.

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<sup>5</sup> Giorgio Sacerdoti. "The United Kingdom's Post-Brexit Trade Regime with the European Union and the Rest of the World: Perspectives and Constraints." *Journal of International Economic Law* (2017).

<sup>6</sup> Ibid.

### **The Economic Impact and Trade Figures – Statistical Analysis**

The continuous study and deliberation revolve around the economic ramifications of Brexit on global commerce. Although detailed data on the exact effects of Brexit on trade flows is still being developed, there are significant patterns:

The Office for National Statistics (ONS) reported a 14.9% decline (£18.9 billion) in UK goods exports to the EU during the first quarter of 2021, as compared to the corresponding period in 2020.

According to the Office for National Statistics (ONS), there was a 20.3% decrease (£23.7 billion) in UK imports from the European Union (EU) during the first quarter of 2021, as compared to the corresponding period in 2020.<sup>7</sup>

The comprehensive ramifications of Brexit on trade and the economy of the United Kingdom will persistently develop as enterprises adjust to the novel trade environment and manage the enduring consequences of the UK's withdrawal from the European Union.

The global trade landscape has been significantly impacted by the Coronavirus pandemic and supply chain disruptions in recent years. However, Brexit has had an extra influence on UK commerce.<sup>8</sup> In recent years, there has been a notable increase in global trade volatility due to the global recession and subsequent rebound following the pandemic, as well as interruptions in global supply networks. The United Kingdom experienced heightened uncertainty due to the protracted and extensive negotiations surrounding the withdrawal arrangements and future trading relationship. This uncertainty was further exacerbated by a significant depreciation of the country's exchange rate, which had already had adverse effects on investment, imports, and exports prior to the formal exit of the United Kingdom from the European Union. The investment growth rate of the United Kingdom had a poor trajectory before to the occurrence of Brexit, a factor that also contributes to the stagnation of productivity development within the country. After the Brexit referendum, there was a protracted period of uncertainty over the relationship between the EU and the UK, which further reduced investment. The diminished appeal of the United Kingdom as an investment hub for international corporations has also had an impact on exports.

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<sup>7</sup> Garcia, Maria J. "Post-Brexit Trade Policy in the UK: Placebo Policy-Making?" 11 Journal of European Public Policy 2494 (2023).

The commercial ties between the European Union (EU) and the United Kingdom (UK) have been regulated by the EU-UK commercial Cooperation Agreement (TCA) from January 2021. According to the TCA, there are no duties or quotas imposed on products exchanged between the European Union and the United Kingdom. In order to be eligible for tariff-free access, UK products must satisfy the rule-of-origin criteria outlined in comprehensive annexes to the TCA. Therefore, in contrast to the Single Market, enterprises encounter supplementary administrative encumbrances and delays at the border due to customs and regulatory inspections. The implementation of the agreement by the United Kingdom and the European Union has occurred at varying rates. EU member states promptly implemented comprehensive customs regulations and inspections on imports originating from the United Kingdom. However, the United Kingdom postponed the implementation of full customs requirements on imports from the EU to the UK until January 2022. Furthermore, the implementation of supplementary health, safety, and security checks was postponed until the conclusion of 2023.<sup>9</sup>

The adoption of the TCA resulted in a substantial decline in UK goods trading volumes with the EU, which remained below their pre-pandemic level until the start of 2022. In terms of imports, it is noteworthy that the United Kingdom had a significant decrease in imports from the European Union (EU) during the initial months of 2021, despite the delayed implementation of Trade Control Act (TCA) regulations. This fall stands in contrast to an increase in imports of products from nations outside the EU. This observation suggests a potential replacement between imports from the European Union (EU) and non-EU countries, wherein products are being rerouted away from transit through EU nations. Nevertheless, variations in cycle patterns throughout the pandemic, resulting from disparities in case counts and limits, as well as varying levels of vulnerability to global supply constraints, may have significantly influenced the situation. In recent months, there has been a reduction in the disparity between imports from European Union (EU) and non-EU counterparts. However, it seems that the influence of these variables has been relatively transient.<sup>10</sup>

Following the implementation of the TCA, UK exports to EU nations saw a significant decline due to the difficulties faced by exporters in meeting the increased paperwork obligations for demonstrating adherence to EU standards. Following this, there has been a partial recovery in

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<sup>9</sup> Ansgar Belke & Daniel Gros. "The Economic Impact of Brexit: Evidence from Modelling Free Trade Agreements". *Atlantic Economic Journal* (2017).

<sup>10</sup> Ibid.

UK goods exports to the European Union (EU) and a subsequent alignment with exports to non-EU partners. However, it is important to note that these exports have remained somewhat restrained in comparison to the patterns observed before to Brexit. Brexit continues to be a significant determinant. Based on a recent poll conducted by the British Chambers of Commerce, which involved over 1,100 enterprises, it was found that 77% of companies engaged in trade with the European Union reported that the agreement did not contribute to sales growth or company expansion. Over 50% of the companies had challenges in adjusting to the new regulations for exporting commodities, with 45% specifically referring to services.

The level of services trade with the EU has been somewhat lower compared to trade with non-EU countries. The majority of the first more pronounced decrease in services trade with the European Union (EU) seems to be attributed to the epidemic, mostly due to the greater proportion of the travel and transport industries in EU trade compared to non-EU trade, as well as the travel limitations imposed during the pandemic. In conjunction with the revival of tourism, the services trade in the UK has rebounded, surpassing the levels observed before the epidemic. This also signifies the surge in travel costs following the outbreak. Exports of financial services to the EU, along with other significant categories of services, had a more significant decline or failed to rise as much as exports to other countries until the end of 2021. These exports have stayed below their levels before the epidemic. The phenomenon of Brexit seems to have exerted an influence, maybe attributable to the absence of agreements pertaining to the trade of services. The provisions of the TCA were restricted in the domain of financial services, which constitute around 20% of the overall services exports in the United Kingdom. The United Kingdom and EU had previously agreed to establish a Memorandum of Understanding on regulatory cooperation, in addition to the TCA.<sup>11</sup> However, this agreement has not yet been signed. The significance of the European Union (EU) as a trade partner for the United Kingdom (UK) has diminished subsequent to Brexit. In 2022, the EU's contribution to the overall financial services exports of the UK was at 29%, a decrease from the 37% recorded in 2019.

Since the establishment of the TCA, the UK's current account deficit has increased, mostly due to changes in the goods balance. The UK current account deficit surged to an unprecedented 7.7%

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<sup>11</sup> Dhingra, Swati, Hanwei Huang, Gianmarco Ottaviano, João Paulo Pessoa, Thomas Sampson, John Van Reenen, Gino Gancia, and Ugo Panizza. "The Costs and Benefits of Leaving the EU: Trade Effects." 92 *Economic Policy Journal* 655 (2017).

of GDP in the first quarter of 2022, primarily driven by a deterioration in both the trade deficit and the income balance. The increase in the trade deficit may largely be linked to the rise in energy costs. However, the decline in the goods balance since the introduction of the TCA has been the primary factor driving the changes in the UK current account. Since the start of 2021, the services balance has been relatively steady, accounting for around 6% of UK GDP. This signifies the conclusion of the preceding pattern of increasing surpluses in the UK services balance.

The commercial recovery in the United Kingdom following the epidemic has exhibited a slower pace compared to other developed countries. Although the United Kingdom saw a decline in exports, like to other nations, during the onset of the epidemic, it derived far less advantage from the following rebound in global commerce. By the conclusion of 2021, the exports of other developed nations had nearly returned to their pre-pandemic levels, although the exports of the United Kingdom remained around 10% lower than that level. Consequently, the proportion of UK trade in relation to GDP saw a fall of 11% from 2019 to the conclusion of 2021, which was notably more pronounced compared to the decline witnessed in the euro area or the United States. By the conclusion of 2022, it seemed that the disparity between UK exports and those of other developed nations had diminished, suggesting that the disruptions associated with the Brexit transition phase are diminishing. Nevertheless, it is important to exercise prudence when interpreting this. This growth may also be attributed to temporary catch-up effects resulting from the epidemic and subsequent fluctuations in trade data in the United Kingdom.

The literature has employed two primary methodologies to separate the influence of Brexit from the consequences caused by the epidemic. A difference-in-difference technique has been employed by several academics, with diverse datasets and specifications.<sup>12</sup> Freeman et al., Du and Shepotylo, and Du et al. conduct a comparative analysis of the development of UK-EU trade in relation to UK trade with other countries. In contrast, Kren and Lawless utilise EU commerce with the rest of the world as a benchmark for comparison.

In this study, we utilise high-frequency product-level data pertaining to trade in products. To account for variations in trade patterns outside Brexit, namely the impact of the COVID-19

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<sup>12</sup> Paolo R. Vergano, Tobias Dolle. "The Trade Law Consequences of 'Brexit.'" 4 *European Journal of Risk Regulation* 799 (2016).

pandemic on trade flows, we employ a complete set of fixed effects for product-time and product-partner. Springford presented many revisions of Brexit effect estimates by employing a "doppelgänger" methodology, wherein an algorithm is utilised to identify nations whose economic performance closely aligns with that of the United Kingdom prior to Brexit. Considering the variations in research approaches, the existing empirical data indicates that Brexit has resulted in a decrease in trade between the United Kingdom and the European Union, both in terms of volume and direction. Table 1 presents a comprehensive summary of current findings derived from several methodologies. The projected decrease in UK commerce with the EU varies between around 10% and 25%.<sup>13</sup>

The findings presented by Springford and Du et al. indicate that the outcomes are contingent upon the specific time frame under examination. Given that both UK and EU enterprises are now adapting to the new circumstances, it is possible that the disparity between estimates could gradually diminish in the future. In addition to offering estimates of the impact of Brexit since 2021, the existing research typically does not discover any indication of anticipatory effects, which refers to a decrease in the share of UK-EU trade in relation to total UK trade before the temporary implementation of the TCA at the beginning of 2021. Brexit has resulted in a substantial decrease in commerce with the United Kingdom across all EU Member States, but with various degrees of impact. The decrease in trade has been particularly evident in nations that have traditionally held a larger proportion of trade, such as bilateral trade with Ireland, exports to Cyprus and Malta, and imports from Belgium and the Netherlands.

There has been a significant decrease in the quantity of items exported from the United Kingdom to the European Union at the product level. Similar patterns are not observed in the exportation of goods from the European Union to the United Kingdom. In general, this observation aligns with the notion that the heightened customs regulations imposed by the European Union (EU) have a more pronounced effect on trade flows of lower value, frequently resulting in the entire cessation of such flows.<sup>14</sup> Simultaneously, there has been a growing trend of export sales being concentrated among a smaller number of larger exporters.

A juxtaposition of these findings with those derived from pre-Brexit analysis indicates that the

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<sup>13</sup> Ibid.

<sup>14</sup> Maria Latorre, Zoryana Olekseyuk, Hidemichi Yonezawa. "Trade and FDI -related impacts of Brexit." 43 *The World Economy Journal*.(2019)

immediate consequences subsequent to the TCA have exhibited greater severity than anticipated. Prior to Brexit, several simulations of Brexit scenarios were conducted using various models, incorporating different amounts of tariffs and non-tariff obstacles.

According to a New Keynesian DSGE model, which assumes a free trade agreement scenario for goods trade with the euro area similar to the terms of the TCA, it was generally anticipated that Brexit would result in a long-term decrease of approximately 3% in total UK exports and imports. This decrease would have minor impacts on goods exports to the euro area, but more significant declines in services exports to the euro area.<sup>15</sup>

Based on the existing facts, it can be inferred that the first negative effect on the export of products from the United Kingdom has been substantial. This shows that UK exporters have had difficulties in meeting the heightened administrative obligations subsequent to the implementation of customs inspections at the European Union border. Given the apparent influence of pandemic-related variables on the advancement of services, it is imperative to do more analysis in order to distinguish the effects of Brexit from the impact of the epidemic on this particular sector.

### **Conclusion**

The post-Brexit era, a recognizable change has come in the functioning of the British economy. Despite the low and slow increase in the UK's revenue, the exit of the UK seems to have economically empowered its citizens and create a more democratic environment within the economy.

The Brexit has had a significant impact on the trade relations between the United Kingdom and the European Union. It has had a visible effect on the declining soft power of the United Kingdom. Alternatively, it has struggled to recover in comparison to many other countries in the post-pandemic 2020's era.

The long-term effects of the Brexit still remain difficult to predict.; however, it is clear that the

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<sup>15</sup> D. Bailey, D.Hearne, D., *et. al.* "People, places and policies beyond Brexit." 18 *Contemporary Social Science*,129 (2023).

Brexit has caused a continental shift in the economic mindsets of the countries in the European Union. Many countries who were formerly considering exit have reconciled with this idea and are trying to increase their importance within the EU; in contrast other countries have reviewed their own situation and are considering such a break from the European Union.

