The Impacts of Brexit on UK Exporting Businesses

A UK Powerhouse report
Spring/Summer 2021

Welcome

A note from Bruce Macmillan,
General Counsel.

Welcome

Welcome to our latest economic report.

Similar to our recent UK Powerhouse studies, this report examines the theme of disruption whilst analysing some of the many challenges and opportunities that UK businesses currently face.

Together with the Centre for Economic & Business Research (Cebr), we've turned our attention to Brexit, and in particular the ongoing impact of the Trade and Cooperation Agreement (TCA) on our regions. We consider what insights the TCA might also offer on the Government's "levelling up" agenda, which is influencing both its domestic and its international strategy.

Our analysis is unique. Rather than look at how the trade agreement affects goods, here we explore the impacts on British businesses which export services and export to the EU. The report also includes legal insights from our lawyers, plus commentary from legal professionals in Northern Ireland and Scotland.

The numerous, individually small but cumulatively large, practical realities of past political decisions on Brexit are now starting to become apparent. There are also pandemic-specific impacts, and the progressive expiry of transitional reliefs to contend with.

This data should now help you to reflect on these challenges and plan ahead, not just for your own business and the locations of its operations, but also those of your key suppliers and customers.

While many specifics remain uncertain, the broad direction of political travel to the next election in 2024 and beyond is becoming increasingly clear. With the help of your economic and legal experts, it's time to think about how to ensure your business is one of those that's "levelled up" and not "levelled down".

I hope you find the report interesting. If there are any issues or areas in relation to Brexit that you'd like to discuss, please do get in touch.

Bruce Macmillan
General Counsel

More about

Executive Summary

This report looks at the impact of Brexit on UK exporting businesses and analyses the 12 constituent regions and countries in the UK, in light of the UK formally leaving the EU on Thursday 31 December 2020.

Disclaimer

Authorship and acknowledgements

This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. The views expressed herein are those of the authors only and are based upon independent research by them. The report doesn't necessarily reflect the views of Irwin Mitchell.

London, May 2021

Brexit And UK Exporting Businesses

How the trade agreement is impacting the UK economy.

Brexit And UK Exporting Businesses

Northern Ireland is the UK's constituent region or country with the highest share of SMEs which export to the EU, at **27%.**

23%

of SMEs in London exported services in 2019

– 1.6 percentage points higher than three years earlier and the highest share of any region. This suggests its services sector is most exposed to Brexit.

THIRD COUNTRY STATUS

The **EU-UK Trade and Cooperation Agreement** doesn't resolve significant regulatory, logistical and administrative barriers to trade arising from the UK's status as a third country now it's left the EU.

£414,400
per SME per year

As well as having the highest share of SMEs that export, London also has the highest level of revenues coming from exporting services abroad, at £414,400 per SME on average a year

The UK formally left the EU, its largest trading partner, at the end of the transition period on Thursday 31 December 2020. This followed the negotiating of a free trade agreement to cover goods.

The agreement, announced on Christmas Eve 2020, ensures that goods won't face tariffs or quotas. This makes the deal most similar to the 'Canada-plus'-style arrangement that some had speculated would be a likely outcome of the Brexit negotiations.

Despite this, non-tariff barriers have come into effect, including extra customs checks and forms.

The level playing field agreement, specified in the deal, ensures both sides commit to upholding their environmental, labour and tax transparency standards.

This means neither side can undercut the other, but it limits the level of deregulation the UK can undertake to increase its competitiveness.

Free movement of services has ended, and British businesses now have to comply with varying rules across member states.

The deal made no ruling on so-called financial services equivalence, which allows financial firms to sell into the EU single market from the UK. As a result, in 2021 we may see more equivalence decisions being made, which could go in the UK's favour or against.

These decisions could also result in the UK being effectively required to sign up to EU financial services rules to get the benefit of equivalence.

Some progress has been made, though. It was announced on 26 March 2021 that the UK and EU had agreed the terms of a memorandum of understanding. But confirmation hasn't been given that this has been signed, or what the specific terms are.

It's anticipated that this memorandum will agree a framework for EU and UK regulators to talk with each other, although actual decisions around equivalence are expected to take much longer.

There remains a considerable amount of uncertainty on the impacts of the UK leaving the EU, and the deal leaves much undecided. For example, regarding finance, the UK could decide to opt for more deregulation and not be granted equivalence by the EU.

There's also no mutual recognition of product standards.

Expert view

“The need for equivalence, or at the very least clarity, on the future relationship in financial services remains a critical concern for the UK. We’ve already seen large tranches of business and transactions moving to EU-based financial institutions.

“A stark example is the shift we’ve seen for share trading to other financial centres such as Amsterdam. This is worrying for London’s status as the premier financial centre in Europe. But the shift is an inevitable consequence of the absence of clarity on the future relationship of financial services between the EU and UK contained in the Trade Agreement.

“The willingness of financial institutions and customers to shift their business should be a stark reminder to the UK Government to prioritise the continued negotiations with the EU.

"The government must ensure that UK financial institutions get unfettered access to EU financial markets and institutions, or at the very least equivalence. Difficulties around permanency can arise with mere equivalence, though.

“The current situation leaves many financial businesses with a lack of clarity on how they might perform their business in the future. It’s also leading to increased costs for many who think the best option is to set up a branch within the EU. The alternative would be to try to seek regulatory approval in each of the remaining 26 jurisdictions.

“To secure equivalence, the EU is likely to demand to be notified and informed of any future changes to the way the UK might regulate financial services. This flies in the face of removing power and oversight from Brussels.

“Many also believe that the UK Government thinks Britain can retain its presence and power in financial services without the need for equivalence.”

Craig Weston
Senior associate barrister and regulatory expert, Irwin Mitchell

More about

Impact On Employment

What effect the new rules are having on the UK jobs market.

Impact On Employment

The automatic recognition of professional standards between the EU and the UK has ended, although a framework could be introduced in the future.

This means that "doctors, nurses, dentists, pharmacists, vets, engineers or architects must have their qualifications recognised in each member state they wish to practice in."

A new points-based immigration system has also been introduced.

Visas giving the right to work in the UK are awarded to those who meet a specific set of requirements.

This means it's much harder to hire workers from abroad, limiting the pool of employees available to UK businesses.

Expert view

“The balance of employers expecting to add jobs was 27% in the second quarter of 2021, and retailers and hospitality businesses are currently planning to hire at the fastest rate recorded in eight years. That’s according to a Chartered Institute of Personnel and Development (CIPD) survey of more than 1,000 UK employers.

“Despite this, there are far fewer non-UK workers seeking employment in the UK or being able to obtain a visa.

“EU individuals who haven’t resided in the UK by the end of last year won’t be able to apply for pre-settled status under the EU Settlement Scheme. These individuals will only be able to come to the UK to work with a sponsored visa.

“One requirement for obtaining a visa as a skilled worker, or in the context of an intra-company transfer, is to pass a certain salary threshold. This rules out visas for employees in lower paid service-led sectors. This means it’s much harder to hire workers from abroad, limiting the pool of employees available to UK businesses.

“There are also limited circumstances in which an EU citizen can come to the UK to carry out temporary business activities without full visa sponsorship. The short-time business visitor visa for up to 180 days is designed primarily for travellers to come to the UK for the purposes of visiting friends and family or tourism.

“But the visa also allows holders to carry out certain general business activities. These include attending meetings and conferences, negotiating and signing contracts and gathering information for their employment overseas.

“The permitted activities are fairly restricted, though. Many EU businesses have found that their ability to provide services in the UK has been severely curtailed by the new Immigration rules.”

Sybille Steiner
Partner and employment expert, Irwin Mitchell

More about

Services Exports

Which regions are being most affected by new rules around exporting services.

Services Exports

This section analyses UK regional data on the share of businesses which export services.

Given the end of the free movement in services, many businesses are likely to be facing a tougher trading environment.

By studying which regions trade most in services, we'll understand the areas of the UK that'll be most impacted by the fallout of the UK leaving the EU.

Figure 1 shows that 23% of SMEs in London exported services in 2019 –1.6 percentage points higher than three years earlier.

This suggests that London is the region most exposed to the effects of Brexit for the services sector.

The Brexit agreement made in December 2020 could cause a potential loss of £9.5 billion (at 2018 prices and level of GDP) per year for the Greater London area. That's according to [previous Cebr research conducted for GLA.]

£2.2bn of this impact comes from losses in the financial services and associated professional services industry.

Northern Ireland and South East England are also highly exposed to restrictions on trade resulting from the Brexit deal. 21% and 14% of SMEs in these regions, respectively, export services abroad.

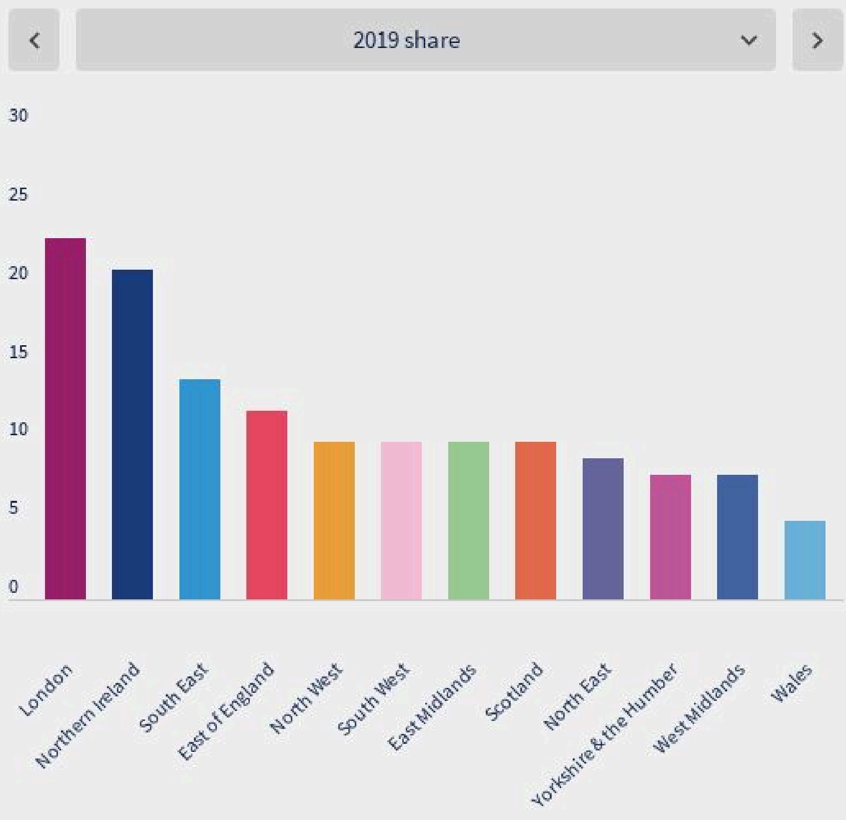
The three least exposed regions to the impacts of the Brexit deal are Yorkshire & the Humber, the West Midlands and Wales.

These regions have the smallest share of SMEs exporting services.

In particular, the West Midlands' larger manufacturing sector makes it more exposed to goods trade.

Businesses operating in this sector will have benefitted from the agreement on free trade in goods, rather than tariffs being implemented.

Figure 1: Share of SMEs exporting services, by region, 2019 and difference between share in 2016 and 2019



Source: Small business survey

Figure 2 shows the average annual turnover SMEs generated by exporting services between 2016 and 2019.

London has the highest share of SMEs that export. It also has the highest level of revenues coming from exporting services abroad, at an average of £414,400 per SME per year.

These revenues are at risk of falling if an arrangement on services exports isn't agreed between the UK and EU.

There were 240,000 SME employers in London at the start of 2020.

Calculations suggest that the 23% of these that export generated a total of £23 billion in revenues from exporting in 2019.

Scotland and Yorkshire & the Humber follow London in terms of revenue coming from exporting services.

They see an average turnover generated by exporting services, for SMEs which export services, of £242,700 and £179,200 respectively, per year per business.

The East of England is the third highest region in England for revenues generated per business for exporting services, at £138,500.

Conducting the same calculation as for London suggests businesses that export services in this region generate a total of £2.3bn in revenues a year.

Figure 2: Average turnover generated by exporting services, between 2016 and 2019, for SMEs which export services, per year per business

Source: Small business survey

Expert view

“Although this report highlights that some areas of the UK are impacted more than others, UK businesses trading with the EU are facing significant disruption as a result of a less free-flowing border.

“Without a doubt, companies have been experiencing the impacts of the transition period ending throughout their supply and distribution chains. Disruption is affecting direct supplies to consumers, as well as supplies of components to manufacturers.

“If your business hasn't done so already, you should audit your supply chain for vulnerabilities to take steps to avoid any adverse impacts on the business.

"This should involve identifying where you receive supplies from the EU, and considering whether an alternative supply route is available

“Organisations that export goods and services should be watching developments closely in relation to new trade deals that emerge with countries outside of the EU. These deals can take time, but can be hugely lucrative.

“Businesses should amongst other things ensure that they have all their ‘ducks in a row’ from a contractual point of view.

“Service sector businesses will need to undertake reviews to assess their contractual and trading arrangements.

"Business should also audit their registered and unregistered intellectual property rights, such as trade mark portfolios, to ensure dual registration post-Brexit is completed where necessary. And businesses should undertake a thorough review and update of their cross-border data transfers and data sharing agreements.

“Post-Brexit regulated sectors may need to keep an eye on divergence between EU and the UK guidance on the outsourcing of significant functions and their materiality.

"These sectors will also need to keep a keen eye on tax, especially tax clauses requiring the customer to be responsible for all taxes and duties, not just sales tax.”

Stuart Padgham
Partner and commercial law expert, Irwin Mitchell

More about

EU Exports

The impact of new trading rules, region by region.

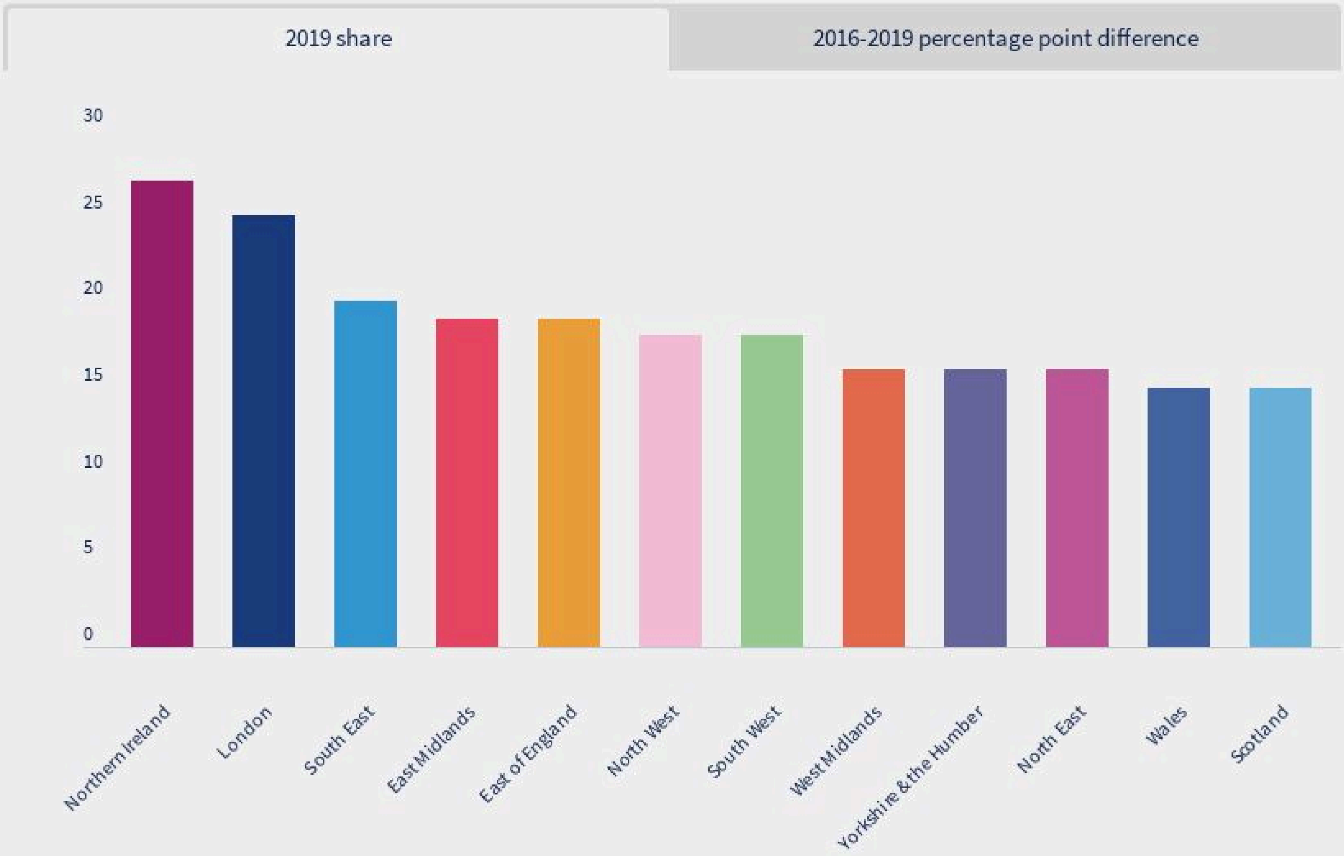
EU Exports

Results from the Small Business Survey, which the data used in this report comes from, also includes data on the share of businesses engaging in trade with the EU.

The survey also details the regional turnover accounted for by exports to the EU.

This can be used to describe the trends in regional UK trade with the EU in the lead-up to Brexit.

Figure 3: Share of SMEs exporting to the EU, by region, 2019 and difference between share in 2016 and 2019



Source: Small business survey

Northern Ireland is the UK's constituent region or country with the highest share of SMEs which export to the EU, at 27%.

It engages in a significant amount of trade with the bordering Republic of Ireland.

London has the second highest share of businesses which export to the EU at 25%, making businesses in the capital highly exposed to the impacts of Brexit on trade.

Expert view

"As a direct result of the Northern Ireland Protocol, Invest NI, the agency of the Northern Ireland Executive responsible for inward investment, has reportedly been inundated with enquiries from manufacturers in Great Britain, the Republic of Ireland, the rest of the EU and around the world about setting up manufacturing facilities in Northern Ireland to avail of the unfettered market access to both the EU and Great Britain.

"Outside of any potential tariff advantage, Northern Ireland is on the right side of the regulatory border for both the UK and the EU. Given the British Government's geo-political commitment to the Northern Ireland Protocol, this advantage for Northern Ireland is permanent.

"By way of example, Northern Ireland manufactured goods will not require both the CE and impending CA marking to sell into both the UK and the EU – the CE will suffice.

"Across the economic spectrum, as Great Britain inevitably begins to diverge its regulatory environment from that of the EU, so the strategic leverage that Northern Ireland possesses as a result of its "two open doors" will grow, incrementally driving its attractiveness as a place for GB, ROI, EU and rest of the world manufacturers to set up in."

Philip Gilliland
Managing Partner, Caldwell & Robinson (Ireland)

Wales and Scotland are the countries least exposed to trade with EU nations, with only 15% of SMEs in each of these countries exporting to the EU.

Scotland has relatively few SMEs which export to the EU. Despite this, it has the second highest average turnover generated by exporting to the EU, at £269,600 per business per year.

Given there are 96,000 SME employers in Scotland, this suggests around £3.8bn in revenues is generated across all SMEs from exporting to the EU. These revenues are at risk as a result of the UK leaving the EU.

Read our exclusive report on how new consumer buying behaviours could transform businesses.

Show me the report

Expert view

“A large part of Scotland’s SME exports to the EU are within the food and drink sectors. Fresh, short-life, produce such as premium seafood and shellfish are often produced by very small businesses, and they have struggled with the additional paperwork required post-Brexit.

“A single lorry load, for example, may contain produce from many suppliers and previously the paperwork was minimal whereas now each supplier must comply. That will reduce exports by those businesses.

“Anecdotally, fishermen from the west coast of Scotland now often land their catches in Ireland, while east coast fishermen land theirs in Denmark. Another quirk of the EU departure arrangements is that there are no transitional arrangements for seed potatoes – a significant crop in parts of Eastern Scotland.

“On the plus side, the easing of the “tariff war” with the U.S. should improve the prospects of the whisky industry, which was previously suffering.

“We have also noticed a small but significant number of factory closures being announced where the ultimate owner has sites in EU locations. It may be that Brexit plus the uncertainty over a second Scottish referendum has given the owners of those businesses the opportunity – or excuse – to relocate.”

John Clarke
Partner, Wright, Johnston & Mackenzie (Scotland)

The East of England is the region of the UK with the third largest turnover per business per year coming from exports to the EU, at £216,100.

The East of England is home to large life sciences and advanced manufacturing sectors.

These will be responsible for a significant amount of exports from the region to the EU.

SMEs in the West Midlands and South East of England see the least revenues coming from trade with the EU, for those which export there, at £126,700, and £122,400, respectively, per business, per year.

Figure 4 highlights the large amount of SME revenues exposed to the trading arrangements between the UK and the EU.

Although the free trade agreement ensured that businesses face no tariffs when exporting to the EU, non-tariff barriers have been introduced which make trade more difficult.

The EU-UK Trade and Cooperation Agreement doesn't resolve significant regulatory, logistical and administrative barriers to trade arising from the UK's status as a third country now it has left the EU. [That's according to a recent report by the House of Lords.]

These new barriers particularly affect smaller businesses and enterprises less accustomed to submitting trading paperwork.

This means that significant trade frictions between the UK and EU have been introduced by Brexit.

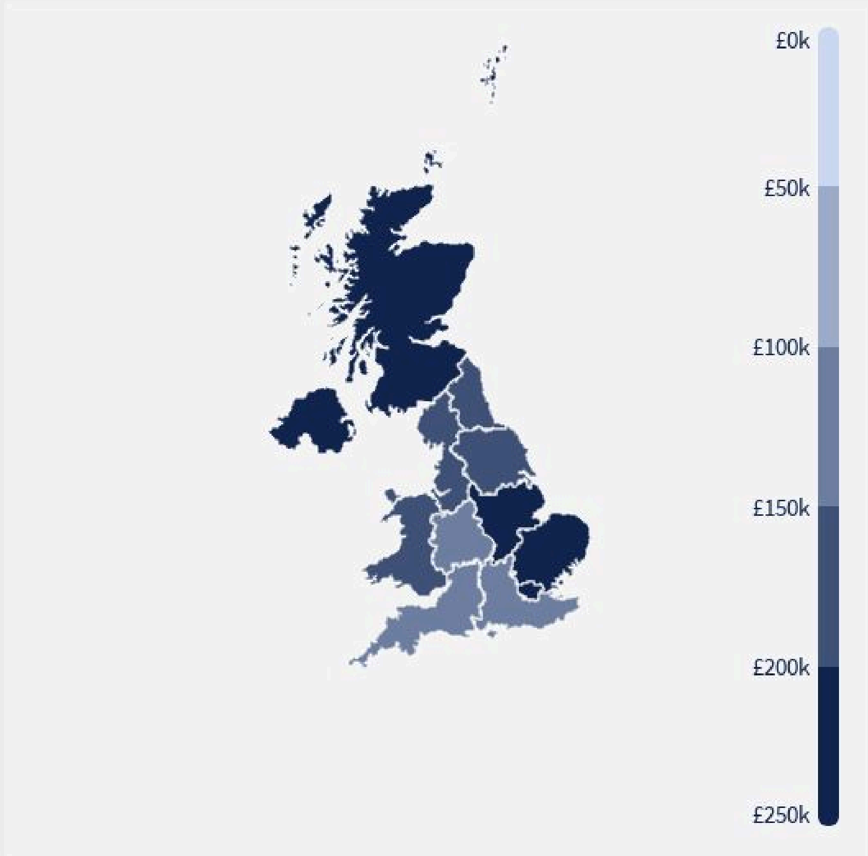
The report also found that businesses trading animal and plant products have been hit hardest by red tape resulting from Brexit.

Many of these products can't be stockpiled, and also face the most stringent checks at borders.

The failure to agree mutual recognition of the procedure for ensuring a product meets necessary regulatory requirements before it's placed on the market is causing further issues.

It could cause duplication of testing of certain products, meaning businesses will incur significant costs.

Figure 4: Average turnover generated by exporting to the EU, between 2016 and 2019, for SMEs which export to the EU, per year per business



Source: Small business survey

As well as complications for businesses resulting from Brexit, many customers have faced problems when purchasing across the EU-UK border.

UK customers have faced a change in the way VAT is collected on purchases from the EU.

For purchases over £135, tax is now collected at the point of delivery, rather than at the point of sale.

Previously, VAT would have been included at the online checkout, but many customers have reported being asked to pay an unexpected charge.

A large volume of UK businesses have revenues stemming from the export of services, which aren't covered by the free trade agreement.

There's also a significant proportion of businesses being disrupted by Brexit border frictions.

As a result, further negotiations between the UK and EU are crucial for sustaining business activity across all UK regions.

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Our experts look at the issues affecting you.

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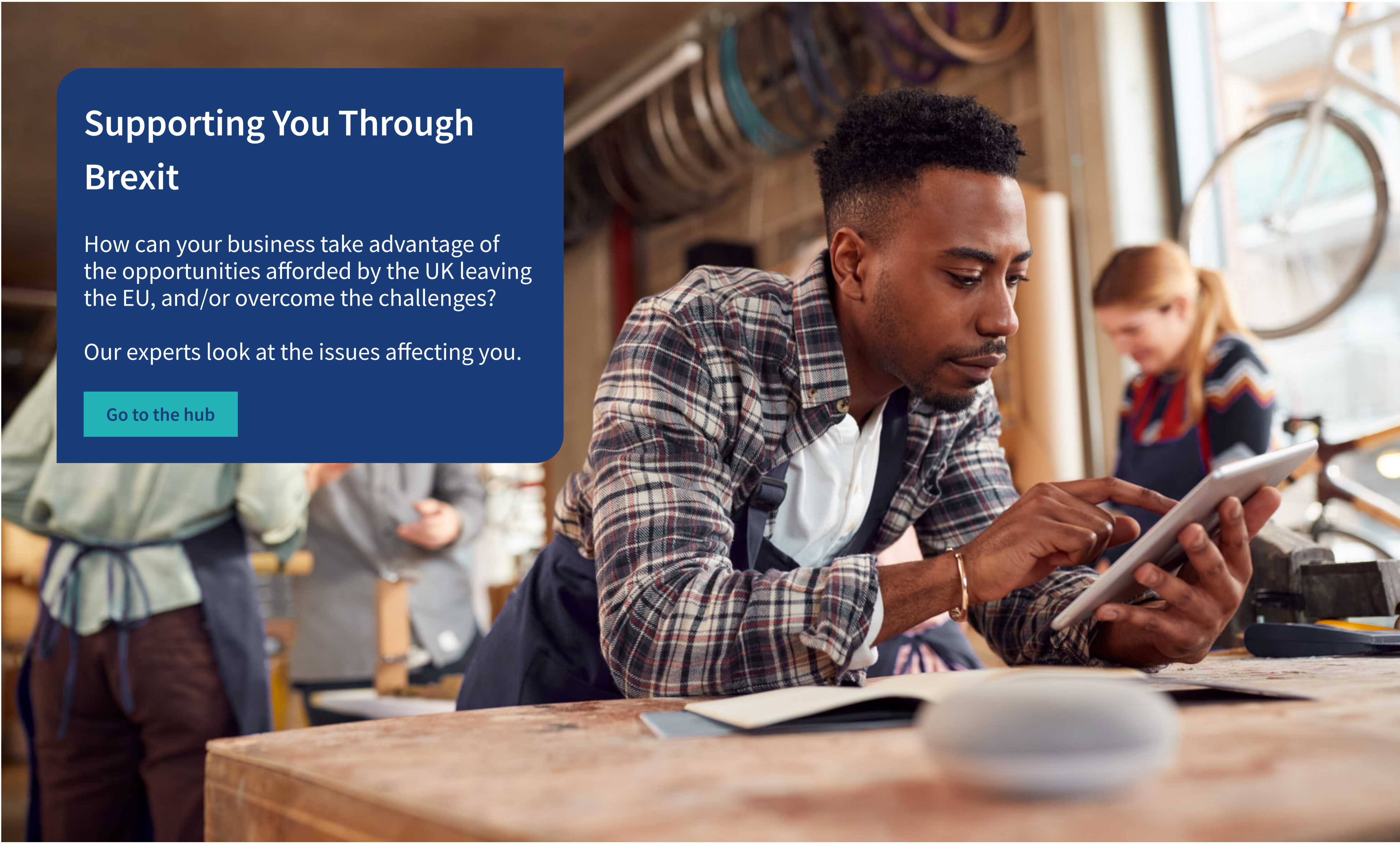

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