Implications for the UK economy since the vote to leave.

In March 2016 prior to the EU referendum, the CBI commissioned PwC to create a report studying the potential impacts of Brexit on the UK economy over the long term to 2030.

The report, rather than forming a part of our central economic forecast, was created to analyse the key channels in which Brexit could affect the UK economy so that businesses could make preparations. This article looks at the key assumptions of the report and the impact on the UK economy since the vote to leave.

- **The report showed that the main channels through which the UK leaving the EU would impact the UK economy would be through uncertainty, higher tariffs, non-tariff barriers and immigration.** It looked at two potential scenarios of the UK economy post-Brexit:
    1. An FTA scenario in which a deal is reached with the EU, based on tariff free trade in goods but not services.
    2. A WTO scenario where the UK does not reach a trade deal with the EU and falls back onto WTO terms

- The report highlighted some potential impacts that these Brexit scenarios could have on the economy:
    1. By 2020, the report suggested that GDP could be between 3.1% and 5.5% lower under the FTA and WTO scenarios respectively compared with remaining in the EU. The largest channel affecting this difference in GDP was expected to be uncertainty following the vote to leave (1.9% - 2.6% impact). The report also suggested that employment could be 550,000-

950,000 lower in 2020 compared to remaining in the EU, under an FTA and WTO scenario respectively.
2. By 2030 uncertainty was expected to be resolved, leaving GDP between 1.2% and 3.5% lower and employment between 350,000-600,000 lower under the FTA and WTO scenarios respectively compared with remaining in the EU.

- Context is important for evaluating the relevance of the report today, particularly the timing of the impacts. **Both Brexit scenarios assumed Article 50 would be triggered the day after the referendum (as the Prime Minister at the time indicated).** This didn't happen, instead Article 50 was triggered almost a year after the vote to leave.

- Additionally, these scenarios did not include an assumption that there would be a significant delay to agreeing a future relationship with the EU after Brexit. **The UK may still find itself in an FTA or WTO scenario but this will happen much later than the assumptions made in our 2016 report.**

- As the UK has not yet left the EU, we are yet to see the true impact of Brexit on the UK economy, which will depend on the future relationship we are able to forge with the EU. **However, the impact of uncertainty on the economy in real GDP terms since the vote to leave is broadly in line with the impact estimated in the CBI/PwC report**, as well as other independent forecasts such as the Bank of England and NIESR, with the level of GDP already around 1-3% lower relative to what was expected before the referendum or a remain scenario. That's equivalent to knocking 0.5pp to 1pp off our growth every year since the referendum.

- We also know that Brexit uncertainty is having a real impact on the economy here and now. This is becoming clearer day by day; official data shows that business investment fell every quarter last year - that hasn't happened since the global financial crisis. And, **the level of business investment is already 26% lower when compared with other recoveries.** This is broadly in line with the Brexit scenario analysis in the PwC/CBI report where investment was expected to be 16-25% lower.

- The UK's labour market has held up well, despite weaker overall economic conditions. That is driven by a number of factors, but we hear from many businesses that they have prioritised holding on to their people where possible, despite the uncertainty and perhaps hopeful that a deal with the EU can be done, unlocking investment potential. However, there is another side to the jobs coin, productivity growth remains well below pre-crisis levels, while businesses are reporting severe skills shortages across sectors. Coupled with data showing weak business investment this implies that there may be some element of substitution of additional labour for investment in capital and upskilling.

- We have recently released our latest forecast for the UK economy, which predicts growth of 1.4% and 1.5% in this year and 2020 respectively. This assumes a withdrawal agreement with the EU is ratified by the end of October. This is why getting a deal is so important for the economy and why the CBI has done everything since the Referendum to try to make a success of Brexit. Leaving with a good deal, one which can pass through Parliament, is acceptable to the EU and protects our economy, remains critical for our future prosperity.

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