Chequers: the Single Market by another name

Why the Chequers plan only compounds the UK's trade disadvantage

Ewen Stewart and Brian Monteith

With a foreword by The Rt Hon the Lord Lilley

GLOBAL BRITAIN

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22 October 2018

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FOREWORD

by The Rt Hon The Lord Lilley

This paper shatters the illusion that Single Market membership has been an irreplaceable boon to British manufacturing. That illusion lies behind the Chequers plan to keep the UK subject to Single Market rues on goods.

I confess that I bear some responsibility for nurturing this illusion. As the Trade and Industry Secretary who implemented the original Single Market programme I frequently lauded its putative benefits. Indeed, the initial idea was sensible. It involved mutual recognition of each member's product standards and removing those that were anti-competitive. So, companies need make only one range for the entire Single Market instead of 28 variants to conform to each member state's rules.

But that benefitted American or Japanese manufacturers exporting to Europe as much as British or German firms exporting within Europe. European consumers benefitted through lower costs. European (and certainly British) firms gained little advantage. UK goods exports to original Single Market countries grew at under 1.0% pa between 1993-2015 whereas our exports to countries we trade on WTO terms with grew three times as much at almost 3%.

Sadly, the Single Market changed from mutual recognition to centralised, uniform and detailed regulation. This helped established firms consolidate their grip on the market by making it harder for new-comers to enter – and burdened companies that only trade within their home markets in addition to those which export.

That may explain why continental industry, which started with a comparative advantage in manufacturing, captured such a strong share of the UK market that is now the EU27's biggest export market.

As the paper makes clear, British manufacturers do relatively much better exporting outside the Single Market. But our greatest comparative advantage lies in services. Over half the value added that Britain exports is in services where we have a substantial surplus world-wide. But again our performance in the Single Market is disappointing. A lower proportion of UK service exports than of goods goes to Europe, where our surplus is modest compared to that with America.

Because services are much less important to other members than to the UK, the EU has made little progress in removing restrictive practices, despite endless promises. One exception is the creation of 'passports' for financial services firms. As Financial Secretary to the Treasury I negotiated the first Directive creating a passport for banks enabling them to operate via a branch regulated by their home country regulator rather than setting up local subsidiaries. I was disappointed a few years later when my Department could not find any British bank making use of passporting. However, since passporting was extended to a wider range of financial activities their use has become extensive.

Immediately following the referendum, concerns about the impact of the loss of passporting on financial services dominated the media. Interestingly, that has subsided. Banks did not protest when the Prime Minister acknowledged that passports would cease. And they scarcely uttered a whimper when Chequers offered to keep Single Market rules for products but sought no continuing access for financial services. City firms have found 'work arounds' for loss of passports and equivalence.   More important, they and the Bank of England have concluded that the City will be better off making its own rules than remaining a ‘rule taker’.

That raises the question: would we not be better off being free to make our own rules on goods as well, rather than be a rule taker?   We would not use such freedom to scrap rules wholesale. But many could be streamlined and above all made less of a barrier to new entrants.

The most frightening aspect of Chequers is that it commits Britain to accept all *future* rules.   Yet Britain is particularly strong in emerging industries like bio-tech, fintech, AI and genetic engineering – where rules have yet to be set. It would be an act of self-harm to allow those rules to be made by countries that lack such industries and often apply extreme versions of the precautionary principle that throttle new developments.

EXECUTIVE SUMMARY

- There is an illusion at the heart of Government that the Single Market is so critical to UK trading and economic interests that the EU referendum result and Conservative and Labour Party manifesto pledges to leave it should be over-ruled by the ruse of adopting a common rule book for goods and most foods under the Chequers proposal.
- This paper shows that membership of the Single Market, or similar, via the Chequers proposal of a common rule book is effectively remaining in the EU in all but name. Moreover it risks permanently locking the UK into the world's slowest growing, most regulatory burdensome and underperforming bloc.
- The UK trades with the world. She has a surplus with the US, the world's most competitive market, and a broadly neutral position with the rest of the world excluding the EU. In contrast the UK has a £96bn deficit with the EU. Is it not odd that the UK can trade well with counties where it has no trade deal yet has a massive deficit where it has a common rule book and so called frictionless trade?
- This paper demonstrates that being a member of the EU 'common rule book' or Single Market harms British trading interests. The Single Market does not play to UK comparative advantage in services but binds us in on goods, where we run a large deficit.
- It demonstrates the clear underperformance of the Eurozone economically which has resulted in UK business voting with its feet by divesting out of the EU into faster growth areas – notably Asia and Australasia.
- It outlines why vested interests support regulation as an anti-competitive tool to the detriment of small and medium sized companies and the consumer.
- We show the major UK trading opportunity is increasingly in fast growing services areas that are often high margin, more immune to developed market under-cutting and enjoying structural growth.
- We demonstrate that while the Chequers proposal is wrapped up in a different language using innocuous sounding words, like *the common rule book,* the legal text is very clear. Chequers means the UK is bound by common rules that exclusively emanate from the EU with the UK having no say whatsoever in their framing. It is not a partnership of equals.
- Chequers is therefore the equivalent of remaining in the Single Market in all but name while abandoning any pretence to take back control of resetting any regulations – thus breaking the spirit of the referendum result and the manifesto pledges of both Conservative and Labour parties.
- The EU has already offered Great Britain a similar deal to Canada. We should bite its hand off.
- This deal must be for the whole UK by including Northern Ireland. The requirement of a frictionless border is another rouse. Northern Ireland already has a border in currency, tax, VAT, certain agricultural standards, social provision, pensions and the like. Canada Plus offers a near frictionless opportunity that is a win-win for both parties.

INTRODUCTION

It is a cliché but Britain is a trading nation. Last year the UK exported £615bn of goods and services to the world. Trade is the lifeblood of the nation and the historic UK referendum vote to leave the European Union of June 2016 provides the first opportunity, since the UK joined the Common Market in 1973, to operate an independent trade policy designed to maximise British opportunities. To put it another way, this is a likely once-in-a-lifetime opportunity to get it right.

BREXIT provides a unique opportunity to re-boot UK trade and the UK's opportunities for future prosperity by re-taking control of trade policy. What we do with those tools will be a major determinant of growth going forward. Brexit is not a panacea in itself. It will be a success if we can adopt the right micro- and macro-economic policies and trading relationships. History will judge it a failure if we do not.

This paper is designed, using official data provided by the ONS Pink Book on trade and EuroStat, to provide a route map to securing the right trade deal for Britain and indeed the EU.

To do this we highlight the current trading and asset balance sheet patterns, the balance of UK trade and comparative advantage, coupled with an analysis of where the opportunity lies. We examine the reasons for the continuing and growing asymmetry in trading with the EU and the rest of the world and we draw conclusions as to what a good trade deal might look like.

THE PROBLEM WITH CHEQUERS

The Remain camp, including our then Prime Minster, David Cameron, was very clear. A vote to leave would mean leaving the entire EU structure that they said included the Single Market and Customs Union. This in itself was an obvious consequence, as to remain in the Single Market would not really be to leave at all, as the vast majority of EU regulations are Single Market related . To remain in a common rule book would inflict on the UK a scenario where she took virtually all the rules without a say, hardly what was promised and surely the complete antithesis of "taking back control".

It is thus disingenuous of the remain leadership now to claim that voters did not know what they were voting for and it was not clear that Brexit would mean leaving the Customs Union. There is a very large body of written and verbal evidence from the remain campaign and indeed subsequent manifesto commitments from both the Labour and Conservative parties that the UK would leave the EU Single Market and Customs Union. Sadly the Chequers proposal does not remotely meet the referendum or manifesto commitments given by either the current Prime Minister, or Leader of the Opposition.

The Chequers proposal may be wrapped up in a different language using innocuous sounding words, like *the common rule book,* but the legal text is very clear. Chequers means the UK is bound by common rules that exclusively emanate form the EU with the UK having no say whatsoever in their framing. It is not a partnership of equals.

Should it be agreed, Parliament would effectively be forced to accept, apply and obey whatever the EU proposed and *de facto* bound with any rulings by the European Courts of Justice (ECJ). While the current UK influence in agreeing regulation is minimal (the UK has an 8.4% share of the vote in the Council of Ministers) Chequers reduces that to zero. Thus Chequers is effectively remaining in the

Single Market in all but name while abandoning any pretence to take back control of any setting of regulations – thus breaking the spirt of the referendum result and the solemn election manifesto promises.

Moreover, under Chequers there is no ability for the UK to repeal any existing EU law in the fields of the Single Market, agricultural, environment, climate change, social welfare, employment and consumer protection.

The proposal makes clear the UK would not be allowed to reduce regulation below the EU level as a minimum, thus negating one of the principle benefits of Brexit – the ability to fame our own laws and reduce burdensome and anti-competitive regulation. Given that these areas account for virtually all EU statute law it is hard to see how Chequers in anyway means leaving the EU in any meaningful way at all.

The proposal does say Parliament could chose not to incorporate new EU law into UK law, but that the UK 'recognises this would have consequences.' Given the UK would have promised to maintain a common rule book, and a so-called frictionless border with the Irish Republic, it is very hard to envisage any scenario where the UK could legally take such an action as we believe the authors of the proposal well know.

Theoretically the UK could sign trade agreements with third parties but who would wish to do that with a country bound by the rules of Brussel's? Negotiations would have little meaning and there is almost no scope to deliver.

If Chequers forms the basis for an agreement with the EU we believe the UK's body of law will be barely one jot different from the EU acquis in five years' time. Moreover, as it is proposed Chequers will be enshrined in international law, future Parliaments will have virtually no realistic legal ability to revisit this.

What makes the Chequers proposal worse is that its compromises are so needless. The UK's government is caught in the headlights of continuing establishment campaigning that accepts membership of the Single Market is so critical it must be preserved *despite* the referendum and manifesto outcome. This paper will clearly demonstrate this is a major fallacy that needs challenging as under the current arrangements the UK's trade is being materially hamstrung. The Single Market and its common rule book are not blessings but form a curse.

Locked into the failing EU 'Single Market' and its *common rule book* the UK has run up a huge and growing deficit with the EU. Despite this we are able to run a surplus with the rest of the world. This seems paradoxical – we are failing where we are tied in to the EU structure, currently legally – and yet succeeding with the rest of the world where we are not.

The Single Market is the world's slowest growing bloc. That has been the case for a generation now. It is highly regulated and has failed to play to the UK's strategic advantage – services. This has cemented a perpetual and growing UK trade deficit with the EU.

The EU's economic underperformance is due to many factors but one of them is the extraordinary burdensome and bureaucratic regulatory framework EU companies and consumers are forced to adopt. Remaining in that structure will make it almost impossible to strike beneficial trade deals while maintaining significant additional costs to consumers. Moreover, regulatory creep goes well beyond smoothing frictionless trade into areas like the environment, employment law and social protection, all areas the UK Parliament would be much able to legislate for effectively.

It is critical to understand that one does not need to be *inside or part of* the Single Market to trade with it. It is an enduring fallacy that Single Market membership enhances trade – it does not. All countries, with a tiny number of exceptions of those under sanction (like Syria or North Korea) have full *access* to the Single Market.

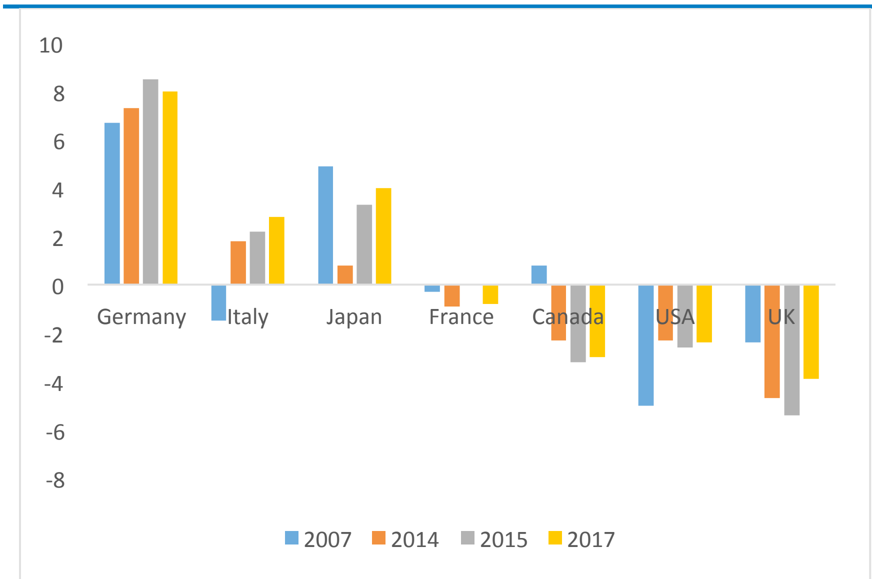
Take China for example, it is not a member but enjoys growing trade with the EU, as does the US and Australia. Indeed none of those examples have any special trade deals with the EU but trade flows freely under World Trade Organisation (WTO) guidance. All of them can trade freely with any EU nations. Yes, all counties need to comply with Single Market regulation, just as all countries, exporting to China have to accept its local standards, but it is absolutely the case that there is open access to trade for all nations outside the EU, or European Economic Area (EEA) structures.

THE UK HAS A TRADE PROBLEM

While the UK's trading performance has improved, over the last couple of years, with the current account deficit reducing from 5.8% GDP to 3.9%, the UK continues to runs a significant deficit, which remains the most serious in the G7 (Figure 1).

This is important as it has long term implications for the level of Sterling relative to other currencies as well as long term growth prospects. While countries can and do run deficits for years, ultimately a nation needs to 'pay its way in the world.'

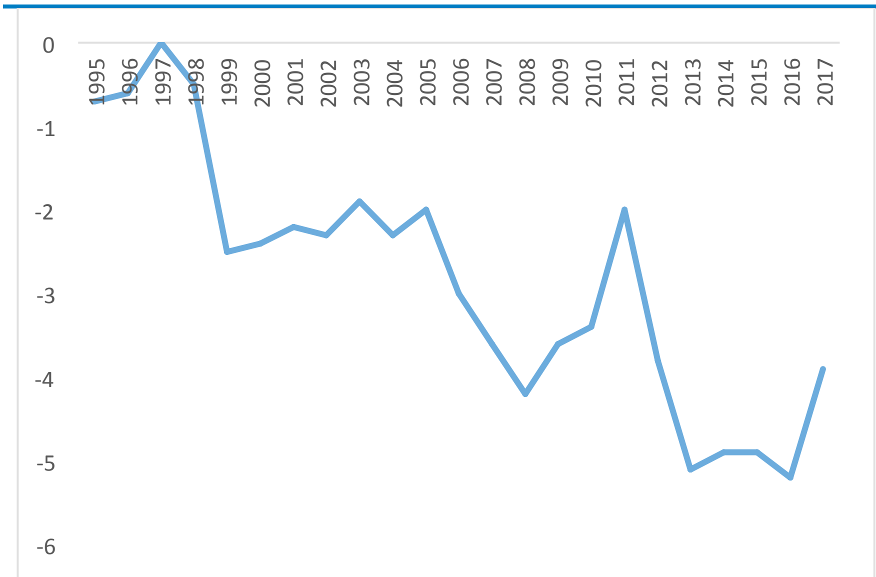
Figure 1: Current account balances of the G7 economies, 2007, 2014, 2015 and 2018 percentage of nominal GDP



Source Pink book 2018

The UK's trade deficit is not a new phenomenon. Indeed over the last 20 years the UK has consistently been in deficit, however the magnitude of this deficit has escalated significantly over the last few years as can be seen from the chart below.

Figure 2:UK Trade Balance 1995-2017 % GDP



Source Pink book 2018

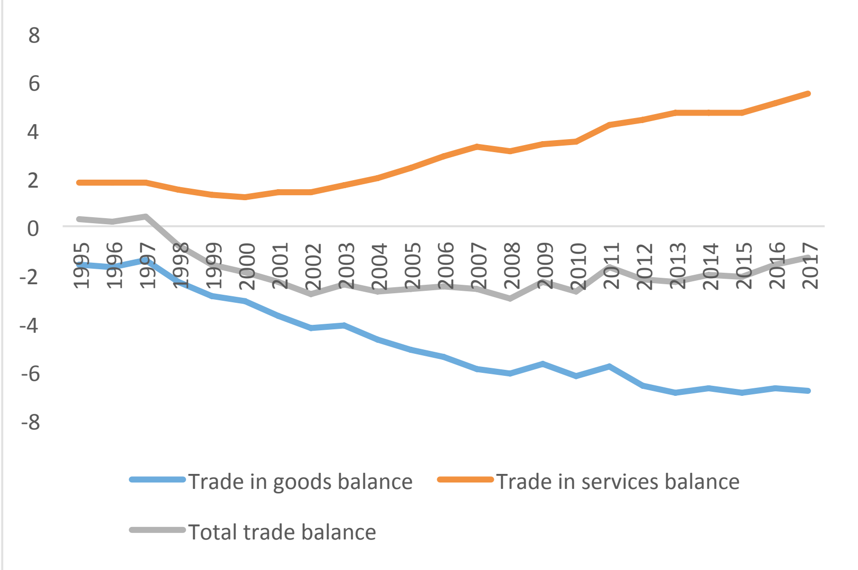
We shall demonstrate that the trade problem is almost exclusively with the EU. The UK broadly pays its way with the rest of the world but runs consistent massive deficits with the EU. Indeed in 2017 that EU current account deficit amounted to £96bn, or almost 5% of GDP.

Does it not strike the reader as odd that despite the EU's snail's pace at negotiating trade deals, (the EU has relatively few compared to countries such as Switzerland and Chile) and the absence of free trade agreements, the UK can run a surplus with the US and Australia and be broadly in balance with the rest of the world – and yet runs a very substantial deficit with our neighbour, the EU, where we have complete regulatory alignment, a 'common rule book' if you like, in the EU Single Market? Surely that alignment would give us an advantage to perform better than we do with others where it does not exist? So how can this be? There are three major asymmetry's that explain it.

Asymmetry One – The UK is good at services, not so good at goods

The UK's balance of trade is heavily skewed, as can be seen from the chart below. The UK runs a significant and growing trade surplus in services offset by an even more significant deficit in goods. We know of no other developed nation with such an imbalance: plus 5.5% on services, minus 6.8% on goods.

Figure 3: UK trade in goods and services balance, current prices, 1995 to 2017, percentage of nominal GDP



Source Pink book 2018

Moreover, given the tendency for excellence clusters to develop geographically, the likely direction of UK investment, and existing strategic advantage, we expect the dependence on services, relative to goods, to increase further over time.

This is not, in our view, a cause for concern. It is arguably a strength, as globally service exports tend to be 'higher added value' and less prone to low cost labour markets undercutting higher cost Western suppliers.

Further as developing markets grow they tend to move up the import curve from basic manufactured product to a greater propensity to consume services, examples of this include financial services, legal services, logistics and IT, cultural and media assets and the like – all of which add significant value, are generally high margin and in structural growth. This trend to service growth bodes very well for the UK in the longer term, particularly in an age of globalisation where there is generally 'goods' price deflation.

The table below clearly demonstrates the asymmetry. A £96bn current account deficit with the EU, £14bn deficit with EFTA and a £16bn deficit with Asia matched £34bn surplus with the Americas and a £13bn surplus with Australasia.

Figure 4: UK trade balance by category £bn

	Goods	Services	P'mary	Secondary	Current Accnt
EU	-95056	28032	-20099	-9085	-96208
EFTA	-18000	9574	-5891	51	-14266
Americas	12500	33878	-12734	625	34269
Asia	-33549	20221	1551	-4282	-16059
Australasia	2640	3880	6658	-152	13026
Africa	-1732	5157	1671	-5049	47

Source Pink book 2018 [Primary and Secondary are balance of investment income and flows to non governmental agencies/ transfers etc. They are components of the current account together with the trade balance.]

The goods deficit with Asia is understandable, given the relatively low labour costs in much of that continent. Indeed free trade with Asia has increasingly benefited British households materially through greatly reduced pricing of garments, electrical products and other low to mid tech consumables.

It is notable however that the UK records a goods surplus with the America's (largely USA) and Australasia as well as large service surpluses. Given that many multinationals and Government actors constantly argue that the Single Market is critical to the UK's economy does it not strike the reader odd that the UK can run both goods and services surplus with possibly the most competitive markets where the UK has no trade deal, often trading on WTO terms, but manages to rack up a £95bn deficit on goods with the EU where it shares a zero tariff environment and a common rule book?

Superficially this does not make rational sense given the so-called advantage of access to the Single Market and common rule book given our current EU membership. The irony is the UK records a goods surplus with the US, where it has no special deal and massive deficit with the EU where the UK does have a trade deal.

Further, despite having no special trade deal with the US the UK exports £60.7bn of services to the US and enjoys a services trade surplus of over £29.5bn (Source ONS Pink Book 2018). This exceeds the position with the EU, where despite being 'in the Single Market' the services surplus is just £28bn.

Moreover, the UK's service trade surplus with non-EU Switzerland of £8.8bn is over a third of that of the entire EU despite Switzerland having just 2% of the EU's population. Something is amiss. The much-vaunted Single Market doesn't even benefit the UK in its very area of advantage. How can this be?

We would argue it is the case because the 'Single Market' – represented in the form of the common rule book that Chequers seeks to preserve – does not play to UK strengths. It results in conformity in goods with a myriad of petty and often anti-competitive regulations where the UK has a deficit – but where the UK has strategic advantage and a small surplus, in services, the common rule book barely exists. The trade barriers between France and the UK on Government procurement or pensions policy are far greater than for example between the UK and US.

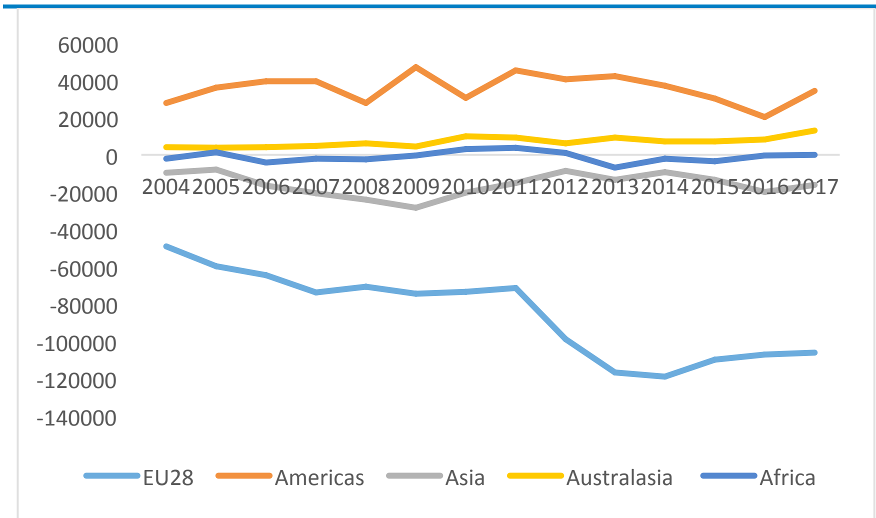
The evidence suggests that the problem of the UK's trade deficit with the EU is a common rule book that weakens our ability to trade effectively and where it is non-existent or hardly developed we trade more effectively. This would explain why the UK can be more successful in trading services to the US, than with the entire EU. The Single Market has been designed to largely benefit the strategic advantage of France and Germany in particular, greatly to the detriment of the UK. The numbers are stark and they speak for themselves.

Asymmetry Two – we do well with the rest of the world and very badly with the EU

Britain competes well with the world. We are able to run consistent substantial surpluses with the Americas (including arguably the world's most competitive market – the US), surpluses with Australasia and a broad balance with Africa. The deficit with Asia is fairly small, at £16bn, when one considers the labour cost competitive advantage the region enjoys.

By comparison the UK's trading performance with the EU is extremely weak with a £96bn deficit in 2015. The UK's trade position has been constantly negative with the EU. However, since 2010 the position has sharply deteriorated. The chart below highlights UK trade performance, since 2004, by region.

Figure 6:UK Current Account trade balance by region £bn



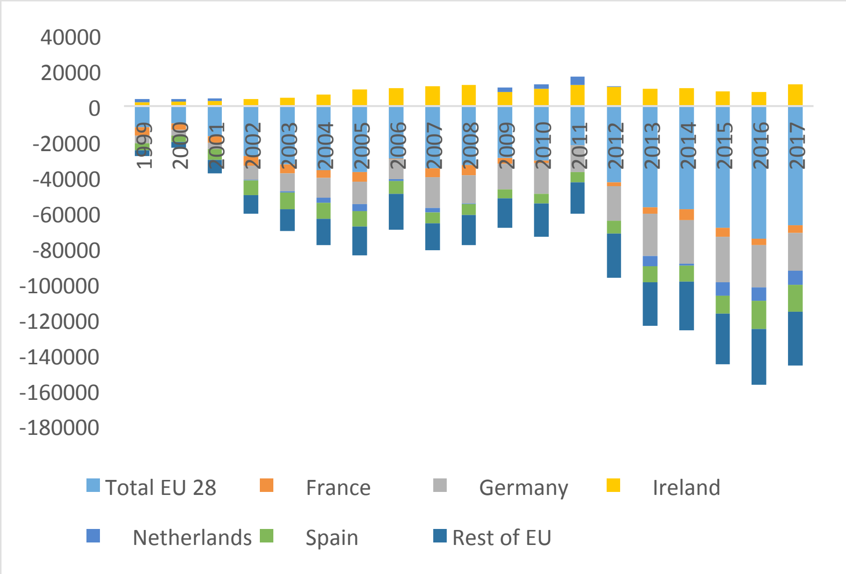
Source Pink Book 2018

The key reason the Chequers proposal, with its rule taking approach, will be so damaging to UK exports, in the long term is it locks the UK permanently into an over-regulated system that favours goods over services.

The system is not designed for UK strategic advantage. It never has been in the forty years of UK membership and given the strengths and weaknesses of France and Germany, the two principle EU partners, it never will be. Thus it is truly bizarre to toss away one of the critical opportunities from Brexit by locking UK trade into permanent underperformance in the European arena.

Further, the UK's trading balance with the EU is constantly poor across the board, the notable exception being the Republic of Ireland where the UK posts consistent surpluses. Figure 7 includes the notable deficits are recorded with Germany (through importing manufactured and engineered goods), France (food, wine, and luxury products), Spain (tourism) and the Netherlands (although in the latter case the Rotterdam effect almost certainly exaggerates the trade statistics.)

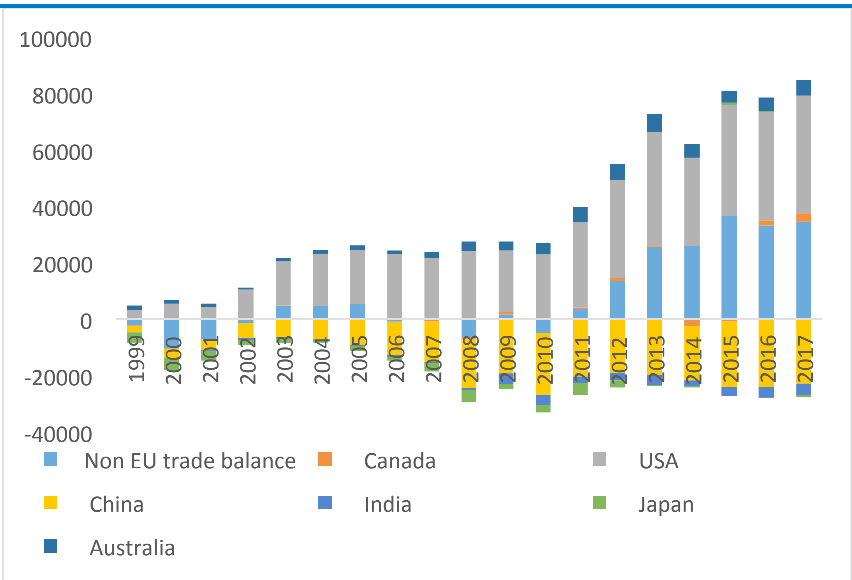
Figure 7: UK trade in goods and services balance with the EU and selected EU countries, 1999 to 2017 £bn



Source Pink book 2018

Contrast this with how the UK performs with other non-EU major global trading partners. With the exception of low cost China the UK more than holds its own against the US, Canada, India and Japan.

Figure 8:UK trade in goods and services balance with selected non-EU countries, 1999 to 2017 £bn



Source Pink book 2018

The great fallacy of trade is that a country needs to be in a Single Market to trade with it. The UK's balance of trade shows this is manifestly not true. The UK does not have to be "inside" the US to trade with it, why then should the UK have to be "inside" the EU's Single Market to trade with it?

It is true that one has to comply with local rules and regulation – and rightly so – but that is not a problem for UK companies trading goods and services with China, US and Australia, three countries where the EU has no formal trade agreement, so why should it be a problem with the EU?

Many politicians have fallen into the trap of believing that membership and proximity are especially important. They are not nearly as important as is often supposed. What generates trade is comparative advantage, innovation and devising products and services that are desired, not reams of regulation, conformity and mercantilism that the EU is so specialised in. This regulatory behaviour only protects existing vested interests, which in the long term stifle the trade and innovation.

Moreover, the EU, by firefighting to preserve the Eurozone increasingly has itself a vested interest that differentiates it from the UK and other Eurozone members. This has begat further regulation, notably in the financial and monetary field directly harming UK interests and productivity.

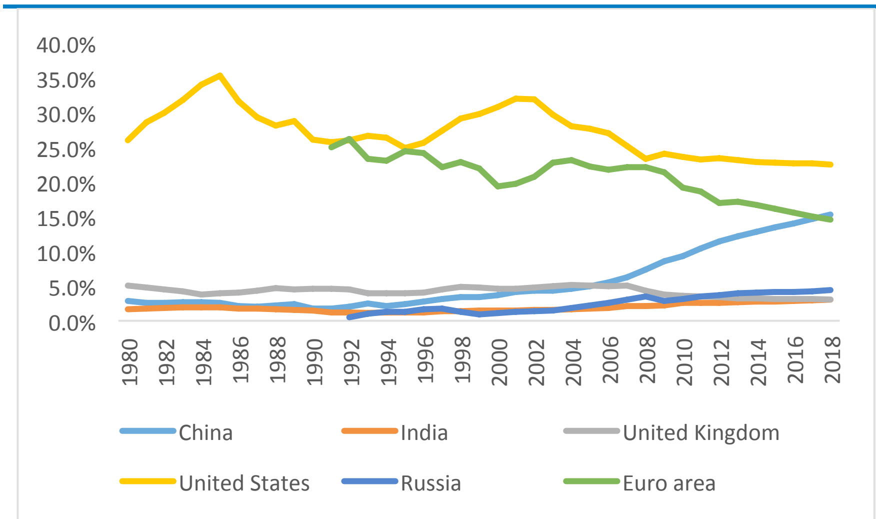
The irony is that, despite a noisy lobby, the UK trades very effectively globally – just not in the EU – proving that the EU system of trade has not worked to UK advantage.

Asymmetry Three – the global size of the EU is in inexorable structural decline

In 1991 the US and European Union combined accounted for 51.6% of global GDP. China's weight was just 1.8%. Today the US and EU account for 39.8% global GDP. China now accounts for 15.5% of the world total, slightly surpassing the Eurozone combined.

As is demonstrated below the US has broadly held global share accounting for just under a quarter of global GDP. The Eurozone, after many year of largely self-inflicted very weak GDP performance, has seen its share decline from 22.1% 10 years ago to just 14.8% today. Current projections are for this to decline to under 10% by 2028.

Figure 15: Share of Global GDP %



Source World Bank

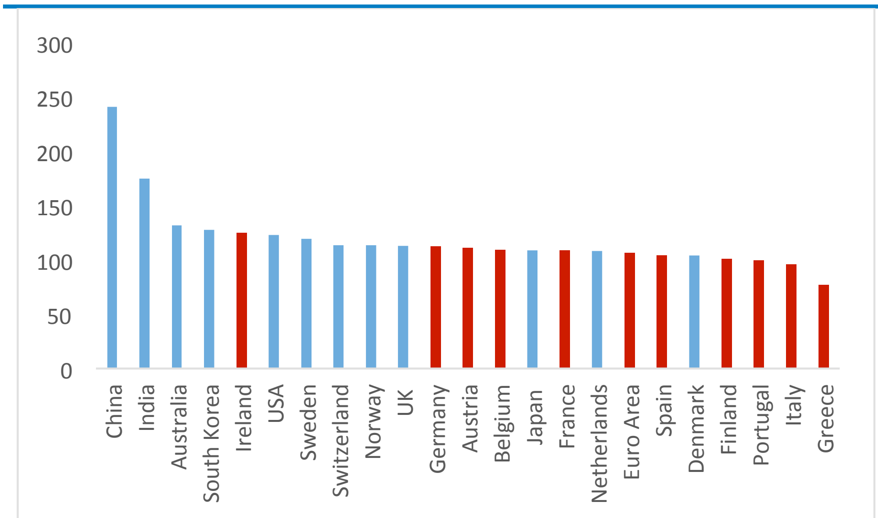
Europe is our neighbour and ally and it will always remain a vital trading, cultural and security partner but, the decline in its importance over the last decade is structural. For the UK, the majority of export growth opportunity will come from outside the EU. This is a near inevitable consequence of demographic change, a GDP catch-up from a low base by developing markets with emerging domestic wealth, and consequent sales opportunities, technology transfer and EU policy failure, notably through the dysfunctional and asymmetric performance of the Euro.

That is not to say that European nations cannot prosper, they can if they adopt reasonably open free market policies, but growth will largely come from elsewhere and UK plc has indeed been following that inexorable trend.

In our view much of the lacklustre performance of the Eurozone is, however, self-inflicted. While this paper is designed to look at UK trade opportunities and not the sub-optimal structure of the Euro, the reality for the currency is the inherent contradiction within the Eurozone from locking the more uncompetitive nations into perpetual low growth as the safety valve of devaluation is removed. This remains unresolved and in our view will continue to result in unacceptably high levels of unemployment at the EU periphery in the medium term, and continuing long term GDP under-performance. This failure directly impacts UK trade by reducing opportunity given the lack of long term growth.

The table below shows GDP growth, for selected major nations, since 2009. Eurozone countries are in red and generally have lagged UK, emerging market and G7 developed market growth. This underperformance has led to lacklustre UK export growth to the Eurozone.

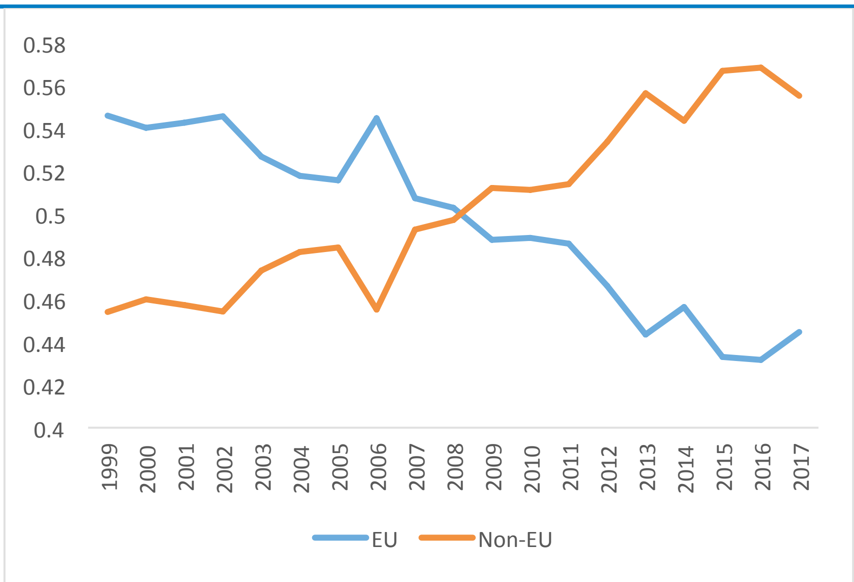
Figure 9: Cumulative GDP 2009-2017 (2009= 100) Eurozone member in red



Source ONS

Shifting global weights and growth opportunity inevitably has had a profound impact on the UK's trading patterns and has resulted in the long drift away from trading with the EU, as our primary partner, as can be seen from the chart below. In 1999 over 55% of UK trade was with the EU. Today that figure has fallen to 43% – as can be seen from the chart below. UK plc is voting with its feet.

UK goods exports to the EU and non-EU areas, percentage of total UK goods exports1999 to 2017



Source Pink book 2018

Given the clear failure of the EU to grow, the scale of the regulatory burden and the UK's strategic advantage in services why does the CBI – and other business organisations and large corporations – support the common rule book of Chequers and de facto Single Market membership?

We believe there are a variety of reasons why there is apparent support by big business towards the EU. Firstly 70% of FTSE 100 company revenues come from overseas. While the US dollar zone is the most important trading factor such an overseas dominance shifts boardroom thinking away from the national to the global. Their policy concerns and resulting lobbying is in Brussels and not the UK. This may favour big business but it does not help the entrepreneurial company or smaller business, let alone the consumer.

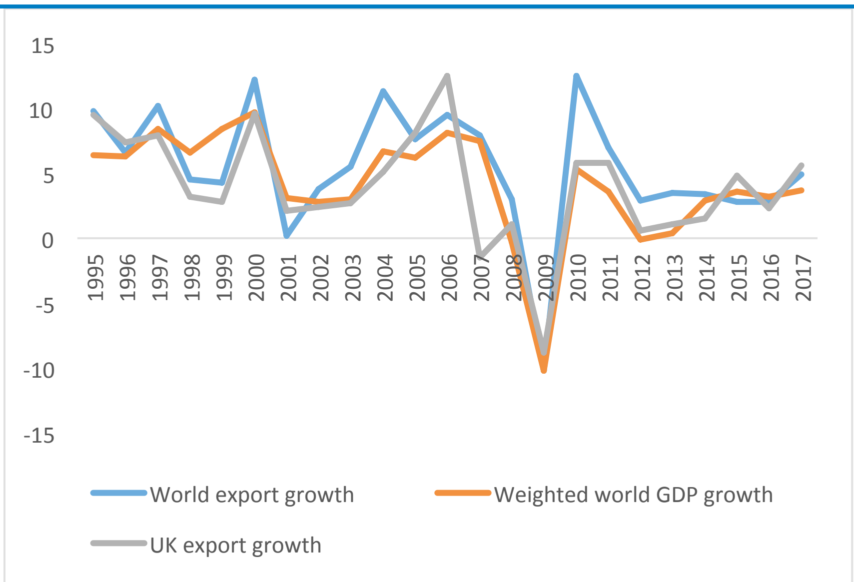
Further, it matters not much to Unilever, for example, if regulation is high and it is doubtless marginally easier to adopt one standard throughout the EU than an individual one for UK consumers. Moreover, many large companies may actually welcome an increasing regulatory burden because it increases the barriers to entry in their industry making it harder for smaller players to compete. While the twin cost to the consumer of excess regulation and reduced completion and choice is substantial it may benefit certain multinational companies. Thus a dangerous gap between the way the CBI and large corporations act and the rest of the population is growing.

It is therefore important to remember, when big business lobby's, that their interest and that of the wider population is greatly diverging and not to the advantage of UK consumers.

TOWARDS FREE TRADE – A MUCH BETTER IDEA THAN CHEQUERS

The poor trading performance of the EU needs to be put in global context. Since the credit crunch global trade growth has been below trend but, at a current 5%, is reasonably robust, as can be seen below. Opportunity is moving East and across the Atlantic.

Figure 11: Annual change in world export growth, weighted world GDP growth and UK export growth, chained volume measure as percentage, 1995 to 2017



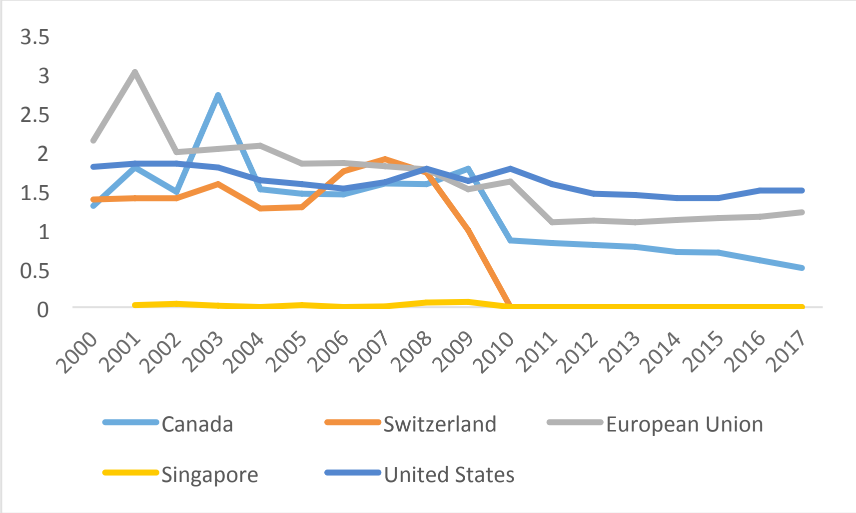
Source Pink book 2018

The outlook for global trade growth remains moderately optimistic, in our view, in the medium term based on global demographics, continuing global productivity improvements, a growing Asian middle class and the artificial stimulus of exceptionally low interest rates.

However one of the critical factors behind a strong global trading environment is the trend towards much lower global tariffs. According to the WTO average tariffs into the EU now average 4% or less and while they remain stubbornly high in certain product lines, agriculture being the primary example, the world is increasingly embracing very low tariffs with a number of countries, Singapore in particular, leading the way with a near zero tariff regime. Low tariffs are good for global growth and low tariffs undermine the *raison d'etre* of being in a customs union like the EU's 'Single Market.'

The EU's record on reaching Free Trade Agreements is very poor. Countries such as Switzerland and Chile having struck more deals and of higher value than the EU and the EU has no FTAs with the leading economies such as US and China and emerging economies such as India. This problem arises because the 28 EU members have been slow to reach agreement, with each having their own special interests they want excluded from any deal. A single country, such as the UK will be able to achieve more FTAs and more quickly than the EU can.

Figure 15: Average Global tariffs



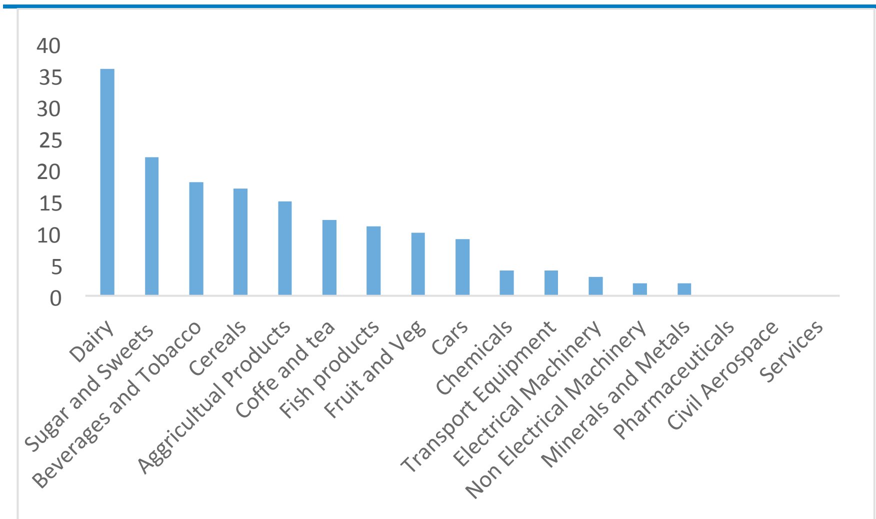
Source WTO

A far better idea than Chequers is to ride the global shift in tariffs downwards and strike out and seek trade deals with the US, China, Australia – *and indeed the EU*. These deals should play to our strengths in services as well as zero tariffs in goods. Far from being at the back of the queue many countries relish the regulatory competition that an unshackled UK could offer.

Where are EU tariffs now?

The chart below shows the EU's current external tariff structure where no trade deal has been struck. In other words this is the WTO option. Outside certain agricultural products tariffs are very low.

Figure 15: EU external tariff structure



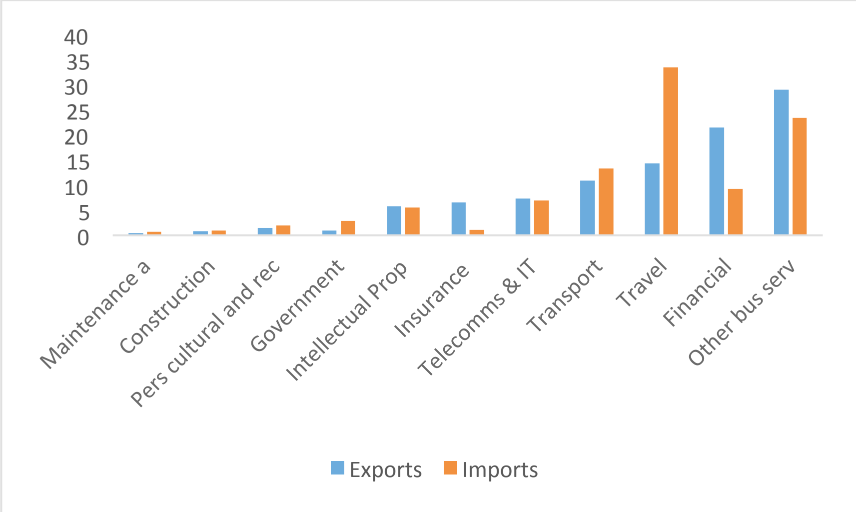
Source Eurostat

Indeed it should be noted that agricultural products imported from Africa and other developing markets are subject to these tariffs currently directly costing the UK consumer and the African farmer dearly. The UK, within the customs union has no ability to vary these tariffs. Under Chequers, or similar derivative that will continue to be the case.

What does the UK trade?

The components of service trade are outlined below but the lion's share of the surplus is accounted for by financial services, partially offset by a large deficit in travel (largely net tourism).

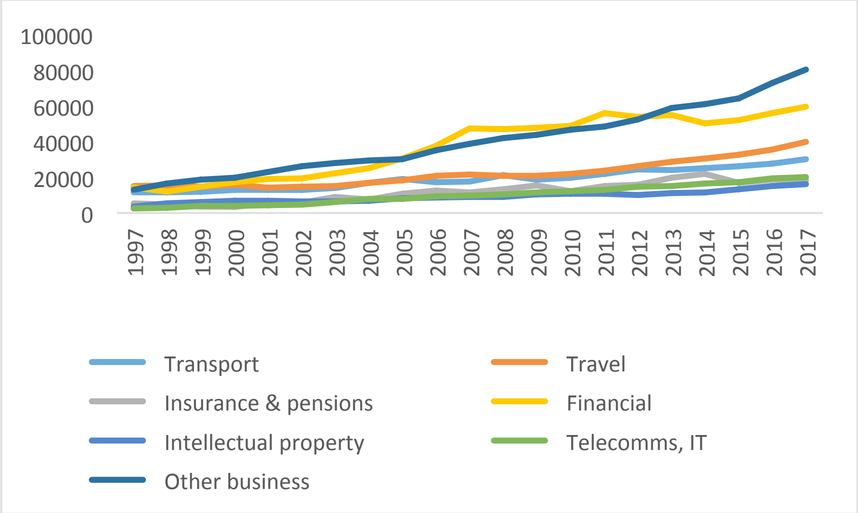
Figure 5: UK trade in services export and import proportions by type 2017 %



Source Pink book 2018

The chart below demonstrates service sector export growth over time with other business services and financial services dominating. The growth in Intellectual property is also noteworthy and we believe it is likely to be a growing area of strategic advantage for the UK given the dominance of UK universities in a European context and a strong performance in culture and media, including games.

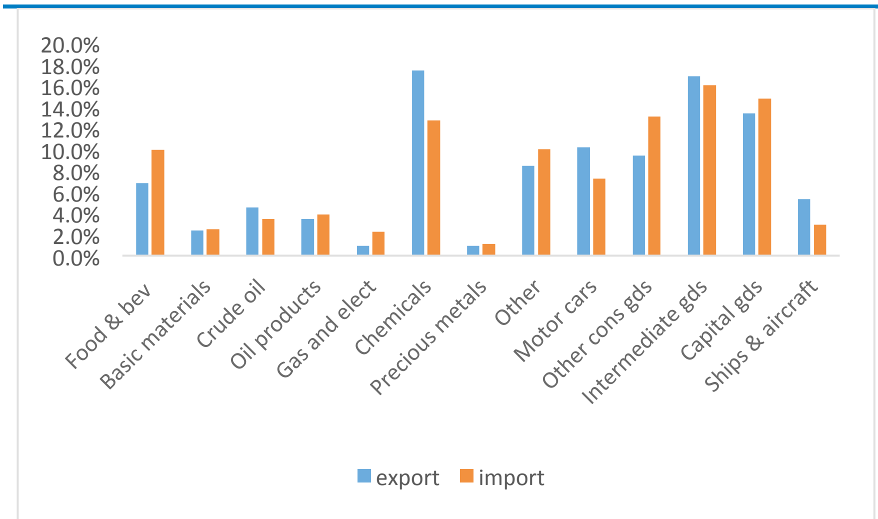
Figure 5: UK trade in services exports £m 1997-2017



Source Pink book 2018

For comparison the chart below highlights the balances in the trade of goods.

Figure 5: UK trade in goods export and import proportions by type 2017 %



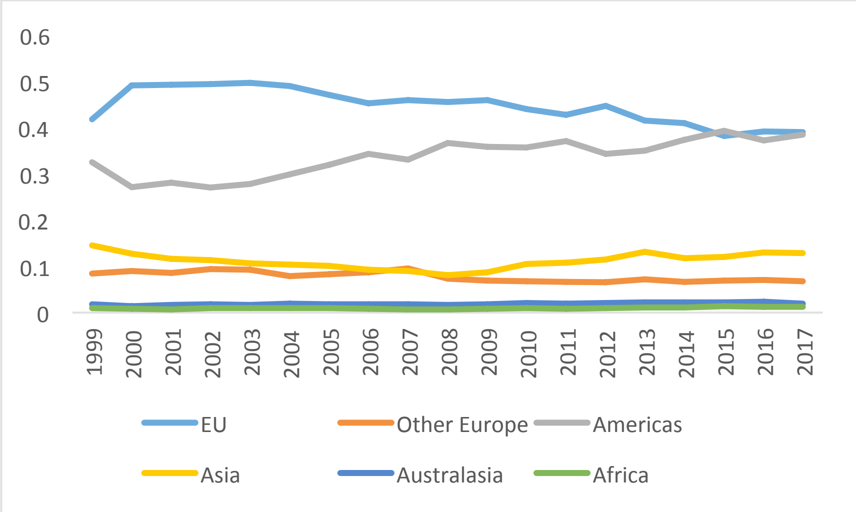
Source Pink book 2018

Where are the assets held?

Trade is a critical part of the mix but if we also examine UK asset holdings we find a similar pattern to trade with the importance of the EU diminishing. While the continent of Europe remains an important home for UK investment as a proportion of total assets held, EU importance has been declining, from 49% of UK foreign assets held in 2005 to 39% today. Most of the growth in overseas investment has been to North America and Asia that together now account for a slightly bigger portfolio investment than our near neighbour Europe. This is demonstrated by the chart below.

Further, absolute investment in the EU peaked in 2008 at £5102bn. The latest data indicates a decline of net investment in excess of £1000bn.

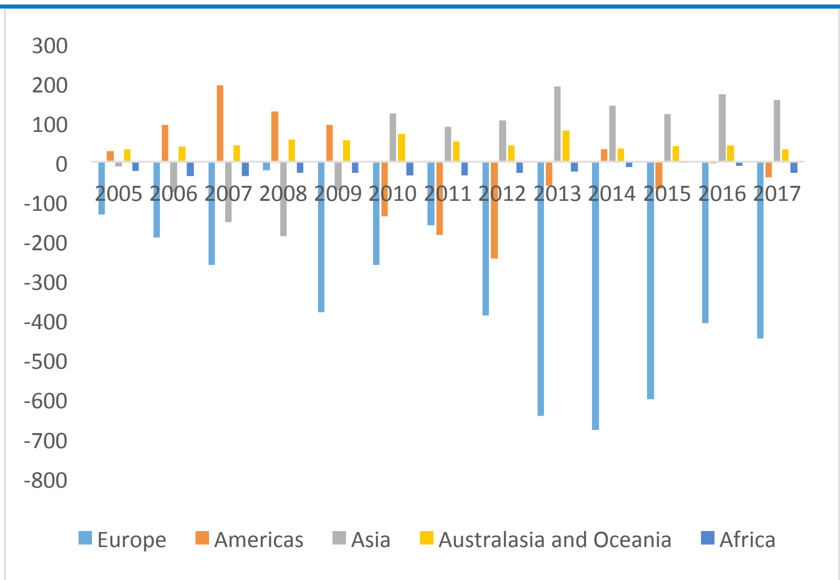
Figure 13: UK foreign assets by continent, £trillion, 2005 to 2017



Source Pink book 2018

The scale of divestment from the EU is staggering. The chart below looks at global flows that indicate global investor unease with EU assets.

Figure 15: Net international investment position by continent, £ billion, 2005 to 2017



Source Pink book 2018

WHY CHEQUERS SHOULD BE CHUCKED

We have demonstrated that the Chequers Proposals effectively mean remaining in the EU Single Market *de facto* and will result in the UK being obliged to incorporate new acquis in all law relating to the Single Market, environment, climate change, social and employment law and consumer protection – leaving little scope to adopt any meaningful independent policy. Worse still, it will all be signed into international treaty making it very difficult to unwind.

We have demonstrated that while maintaining friendly and constructive relations with the EU is manifestly in both parties' interests the EU has been for a generation, and is likely to continue to be for the foreseeable future, the world's slowest growing bloc. Moreover we have, shown that the UK trades in surplus with the US and broadly neutrally with the rest of the world but records a £96bn current account deficit with the EU. It is superficially odd that we can trade just fine where we have no special deal and massively in deficit with the EU where we do. What sort of negotiators would wish to lock us into that sort of relationship in perpetuity?

The UK Government needs to raise its game and quickly. The UK has a unique opportunity to trade freely with the EU and expand our links globally. The often argued objection to a deal similar to Canada – the so called Canada Plus – is that it the EU says it requires a border down the Irish Sea given the UK government's somewhat misguided backstop agreement with the EU.

We consider this to be a fabricated ruse to keep the UK in the Single Market. Sadly, there are clearly those within the British government machine who have latched onto this supposed problem in order to justify remaining inside a customs union and single market. Yet a border between the UK and the Irish Republic already exists at many levels (including currency, VAT, tax, duties, welfare, justice) and ensuring smooth acceptance of standards should not be a problem. The irony, however, is the Irish Republic has far more to lose than the UK if talks fail, given how dependent the Republic is on the UK for trade with 44% of Irish exports going to the UK.

There is a clear route map for a deal and indeed one Donald Tusk, President of the EU Council has regularly offered to Great Britain – it now needs to be offered to the whole of the UK. With goodwill on both sides the Irish issue can sensibly be resolved as the EU well knows.

Moreover, the British population is not impressed. Global Britain demonstrated with one of the biggest opinion polls ever carried out, with over 22,000 voters questioned in the top 44 Conservative marginal constituencies, that Chequers is not only unloved but the population has seen through it as well. The clear polling evidence is the population knows Chequers is Brexit in name only and believes it will be bad for them and bad for the country. It could well cost the Conservative Party power as we have demonstrated that a tiny swing in support shifts the balance to a Corbyn/SNP coalition or a Corbyn victory outright.

The link https://globalbritain.co.uk/brexit-polling/ provides the full polling data set but Chequers is playing with fire. It ties the UK to a failing bloc, makes the UK a rule taker with no say on new law, severely hampers the UK's ability to strike new trade deals and with near certainty ensures that the UK is locked into a system that harms our trading relationships in the long term given it would be enshrined in international law.

On top of this the Chequers proposal is in bad faith as it clearly contravenes the referendum result that was subsequently backed up by solemn manifesto pledges. Ignoring the stated and implicit promises to accept the public's decision and deliver a Brexit that meant leaving the Single Market and Customs Union would do untold damage to the democratic process.

Put simply, Canada Plus forms the basis of an offer. It is a deal that would work for business and plays to our potential. The EU is using the Irish backstop as an method to keep the UK in the Single Market and Customs Union to its advantage – its bluff must be called.

CONCLUSIONS

The key myth propagated in favour of the Single Market is that it is central to UK prosperity. It is not. We have demonstrated that the UK trades well with the world but poorly with the EU. This is odd as the UK has no special trade arrangements with the US, China or Australia but runs a small trade surplus with the rest of the world, but a very large deficit with the very region we have a customs union with – the EU.

The EU is in structural decline. It has underperformed every other region in the world for a generation. This is not a coincidence as other advanced economies including the US, Canada and Australia have powered ahead. It is the institutional arrangements of the EU and the single currency in particular that has resulted in rapid economic decline and socially unacceptable levels of unemployment in much of the EU. The EU's trend towards centralised regulation undermines competition and increases regulatory burden. Within the Single Market framework the UK will continue to be beholden to needless regulation and legal creep as EU lawyers interpret a definition of EU competence well beyond merely trading standards and into to many other areas of national life.

The EU has also failed to sign global free trade deals with the world's most important partners including the US, China or Australia. Inside the EU the UK cannot strike its own deals with the many much faster growing nations. Because the EU is a diverse group of 28 nations agreement is highly problematic and cumbersome, hence the failure to reach agreement. Outside the EU the UK can much more readily strike free trade deals.

It is now apparent from comments from the US, China and Australia and others that far from being 'at the back of the queue' other countries are very keen to strike mutually beneficial free trade deals with the UK. This will allow the UK to rebuild its historic mission of encouraging global free trade that has gone off track over the last 40 years as the UK has surrendered its trade policy, so unsuccessfully to the EU.

It is also a myth that the UK needs to be part of the Single Market to trade with it. This is clearly not the case. All nations have access, outside a tiny number under sanction (North Korea and Syria for example) so long as they comply with local regulations. This is the case the world over. One does not need to join China to trade with it any more than one needs to join the EU.

It is clearly in the EU's interests to agree a zero tariff deal with the UK. There are many reasons for this but the primary one is simply because the EU sells more to the UK than the UK sells to the EU. It would be nonsensical to undermine its own trade particularly at a time when EU growth is so weak.

If, however, the EU refuses to do so within reasonable timeframe, the UK should leave the EU without a formal agreement on 29th March 2019, relying on WTO rules and striking free trade deals with our global partners. This outcome would be far better than what the Chequers Plan offers because the UK would otherwise be saddled with a current marginal influence on Single Market regulation (12% vote in the Council of Ministers) for no say in regulatory framework at all while having to accept free movement of people.

To remain under the jurisdiction of the common rule book, effectively still under EU jurisdiction, having left the EU, is the remain option that delivers a sovereignty illusion – with no say, low growth and a high regulatory burden that would lock in perpetual trade deficits. That is why Chequers must be chucked and Canada Plus used as the template for a new relationship.

About the authors…

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Ewen is an economic consultant having previously been worked for major investment banks in The City as a Strategist. Ewen joined Global Britain as director in 2012 when Brexit was still a concept and has since helped make it a reality.

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COMPANY DETAILS

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