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BREXIT AND THE UK ECONOMY
Centre for Economic Performance report
#GE2017Economists @CEP_LSE election analysis

Leaving the European Union (EU) with no deal in place for future trading arrangements would be the worst-case Brexit scenario for the UK economy. What’s more, just because GDP growth has not declined since last year’s referendum, it would be wrong to think that Brexit is yet to have any economic effects: it has already lowered UK living standards by causing the value of the pound to decline, which has led to higher inflation and lower real wage growth.

These are among the conclusions of a new report from the Centre for Economic Performance (CEP) – the latest in a series of background briefings on key policy issues in the June 2017 UK general election. The CEP report describes alternative post-Brexit futures for UK-EU relations and summarises the economic and political consequences of each option. Among the findings:

- The June 2016 referendum gave a mandate for the UK to leave the EU, but offered no guidance on what form Brexit should take.

- CEP research finds that remaining in the Single Market would minimise the economic costs of Brexit. Leaving the EU without any new deal in place would be the most costly alternative.

- There is not yet any clear evidence that Brexit has affected UK GDP, but this does not mean Brexit has had no effect on the economy. The Brexit vote has already made the UK poorer by reducing the value of the pound.

- Between the referendum and the end of April 2017, sterling depreciated by 13% against the US dollar and 9% against the euro. The depreciation is a signal that expectations about the UK’s future economic performance have deteriorated.

- The depreciation of sterling has hurt UK consumers by increasing the price of imports, leading to higher inflation and lower real wage growth. Inflation has risen from 0.5% in June 2016 to 2.7% in April 2017. Real wage growth has declined from 1.3% in June 2016 to negative 0.5% in March 2017. To date, there is no evidence that the depreciation has boosted UK exports or reduced the trade deficit.

- The Conservatives have pledged to take the UK out of both the Single Market and the customs union, while simultaneously negotiating a new partnership with the EU. Leaving the Single Market would mean the UK experiencing higher trade barriers, lower trade and reduced living standards. The Conservatives would try to mitigate some of these costs through a new trade deal with as few barriers to trade and investment as possible.

- The Conservatives have not ruled out a ‘no-deal’ Brexit, leaving the EU without any new agreement in place. While it is a tautology that a sufficiently bad deal must be worse than no deal, in practice the no-deal outcome, where the UK and EU trade under World Trade Organization terms, is the worst-case scenario for
the UK economy. The economic costs of Brexit are twice as large in the no-deal case than if the UK remains in the Single Market.

- Labour’s plan for Brexit is far from clear, but in many ways it resembles the Conservatives’ position. The only unambiguous difference is that Labour acknowledges that no deal is the worst possible option for the UK. The Liberal Democrats propose that once a new deal has been negotiated, the UK should hold a second referendum to choose between the new deal or remaining in the EU.

Co-author of the report Dr Thomas Sampson comments:

‘Prime Minister May’s decision to leave the Single Market was not an inevitable consequence of the referendum and will increase the economic costs of Brexit.’

‘The Brexit vote has already hurt the UK by reducing real wage growth. More pain is likely in the months and years to come.’

‘Both the Conservatives and Labour have chosen to prioritise taking back control over making Brexit work for the UK’s economy. Inevitably, this choice is bad for living standards.’

His co-author Dr Swati Dhingra adds:

‘Brexit does not simply mean Brexit. What matters, of course, is the content of the withdrawal agreement and of any new trade deal between the UK and the EU.’

‘Leaving the Single Market and the customs union, as the Conservatives have pledged, would mean the UK experiencing higher trade barriers, lower trade and reduced living standards.’

‘Labour would like to remain in the Single Market, but also wants immigration controls, which the EU is unlikely to grant.’

ENDS

Notes for editors:

‘Brexit and the UK Economy’ by Swati Dhingra and Thomas Sampson is the latest in CEP’s #GE2017Economists series.

Objective, brief and non-technical, CEP Election Analysis is a series of background briefings on the policy issues in the June 2017 UK General Election.

This series discusses the research evidence on some of the UK’s key policy battlegrounds, including education, health, immigration, industrial strategy, living standards, regional policy and Brexit.

These analyses are provided by some of our expert researchers and draw on some of our past and current research.