A dramatic fall in the value of UK imports from the European Union relative to the rest of the world occurred when the post-Brexit Trade and Cooperation Agreement came into effect. What’s more, according to research by Rebecca Freeman, Kalina Manova, Thomas Prayer and Thomas Sampson, the stability in relative export values conceals the destruction of many smaller trading relationships.

Trade disruptions in the wake of Brexit

The UK voted to leave the European Union (EU) in June 2016, but its trade relations with the EU did not change until 1 January 2021 when the Trade and Cooperation Agreement (TCA) came into effect. Under the TCA, UK-EU trade remains tariff and quota free, but the UK is no longer a member of the EU’s single market or customs union. Consequently, the TCA has increased trade costs between the UK and the EU.

We study both the period between the Brexit referendum in 2016 and the end of 2020 when there was uncertainty over what form Brexit would take, and the first year of trade under the TCA.

We find no evidence that Brexit reduced the UK’s trade with the EU relative to the rest of the world prior to the implementation of the TCA. But the introduction of the TCA resulted in a major disruption of UK-EU trade.

We estimate that the implementation of the new trade relationship led to a sudden and persistent 25% fall in UK imports from the EU, relative to the rest of the world. In contrast, we find a smaller and only temporary decline in relative UK exports to the EU. Nevertheless, there was a sharp drop in the number of trading relationships between UK exporters and EU importers, which suggests that the introduction of the TCA caused many UK firms to stop exporting to the EU.

How do we reach these conclusions? The main challenge is to disentangle the Brexit effect from other causes of changes in trade. For example, if the Covid-19 pandemic caused import demand to fall more in the EU than in the rest of the world, the UK’s relative exports to the EU may have declined for reasons unrelated to Brexit.

Isolating the Brexit effect

To address this challenge, we compare growth in the UK’s trade with the EU to the UK’s trade with the rest of the world, and to US and EU trade with countries other than the UK. This approach allows us to account for changes in exporter supply and importer demand conditions in the UK and abroad and, consequently, to isolate how Brexit has affected relative UK-EU trade.
In addition, to ensure that our estimates are not biased by changes in the sectoral composition of trade, we use product-level trade data for around 1,200 products.

Figure 1 shows our main results for UK exports to the EU – Panel (a), and UK imports from the EU – Panel (b). For each quarter from 2013 Q1 through 2021 Q4, we plot the estimated percentage change in the UK’s trade with the EU relative to the rest of the world, compared with the pre-referendum period of 2016 Q2. The shaded area shows the 95% confidence interval for the estimates, to indicate the degree of uncertainty about their precision.

Panel (a) shows that, although relative exports to the EU fluctuate from one quarter to the next, there is no sign that Brexit has led to a sustained change in the geography of UK export values, either following the referendum or after the introduction of the TCA. Total UK export growth compared with that of other advanced economies was weak in 2021, but our analysis suggests that this weakness cannot be explained by a decline in relative exports to the EU.

Turning to UK imports, Panel (b) shows that, except for a temporary dip at the onset of the pandemic, relative imports from the EU were unaffected prior to the introduction of the TCA. On the other hand, the introduction of the TCA led to a deep and sustained fall in relative UK imports from the EU. UK imports from the EU abruptly declined by about 25% more than UK imports from the rest of the world after the TCA came into effect, and this decline persisted throughout 2021.

It is surprising that the TCA had a greater effect on imports than exports in 2021, particularly since the UK delayed the introduction of many customs checks on EU imports until 2022.

Broken relationships

Further analysis shows that the implementation of the TCA has reduced the number of trading relationships between the UK and the EU. Figure 2 plots the estimated effects of Brexit on the count of products traded with each country in the EU per quarter, using the same approach as in Figure 1 to isolate the Brexit effect. Goods are classified using 6, 8 or 10-digit codes. We count relationships using 8-digit products – an example would be “umbrellas having a telescopic shaft (excl. toy umbrellas)”.

The TCA led to a fall of around 30% in the number of export relationships (or export “varieties”) with the EU relative to 2016 Q2.

Notes: Panels (a) and (b) plot the estimated percentage change in UK exports and imports with the EU versus the rest of the world relative to 2016 Q2.

There has been a steep decline in the number of UK to EU export relationships...
Figure 2: Number of UK trade relationships with the EU versus the rest of the world

(a) Export varieties

(b) Import varieties

Notes: Panels (a) and (b) plot estimated percentage changes in the number of UK trade relationships with the EU versus the rest of the world relative to 2016 Q2. A trade relationship (or variety) is defined as a CN8 product traded with a partner country in a quarter.

This article summarises ‘Unravelling Deep Integration: UK Trade in the Wake of Brexit’, CEP Discussion Paper No. 1847.

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There is no sign that Brexit has led to a sustained change in relative UK export values to the rest of the world and a smaller, but still significant, drop in the relative number of import relationships. The decline in export relationships is driven by the exit of low-value relationships.

The results in Figure 2 imply that the apparent stability in the relative value of UK exports to the EU under the TCA masks a steep decline in the number of export relationships. Consequently, it would be a mistake to conclude that UK exporters were unaffected by the introduction of the TCA. Instead, we conjecture that the TCA has increased the fixed costs of exporting to the EU, causing small exporters to exit small EU markets, but not (or at least not yet) severely hampering exports by the large firms that drive aggregate export dynamics.

Although our analysis provides a rich picture of how Brexit has affected UK trade so far, some caveats are in order. We only study the first year of trade under the TCA, we only consider trade in goods, and our estimation strategy is designed to capture the direct effect of Brexit on the UK’s trade with the EU relative to its trade with the rest of the world. We do not analyse whether Brexit has indirectly affected the UK’s trade with the rest of the world through general-equilibrium adjustments or supply-chain linkages. We plan to update our findings and expand our analysis along these dimensions as more data become available.

Notes: Panels (a) and (b) plot estimated percentage changes in the number of UK trade relationships with the EU versus the rest of the world relative to 2016 Q2. A trade relationship (or variety) is defined as a CN8 product traded with a partner country in a quarter.