



Trade and Cooperation Agreement – London impact

A Cabr report for GLA

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1. Introduction

The EU-UK Trade and Cooperation Agreement came into force on 1st January 2021, as the UK left the EU and following the end of the transition period. The deal ensures that goods traded between the EU and UK won't face tariffs or quotas, yet non-tariff barriers have been introduced, and free movement of labour has ended. Furthermore, free trade in services has ended, which has consequences in particular for London and its large professional and financial services sector.

This report analyses the effects of the UK leaving the EU under the terms of the Trade and Cooperation Agreement, looking at how the size of London's economy will be impacted. It is primarily based on previous work conducted by Cebr for LCCI in 2018.¹

¹ <https://www.londonchamber.co.uk/LCCI/media/media/Brexit-and-the-Metropolitan-Areas-FINAL.pdf>

2. The sectoral breakdown

This report divides the London economy into five sectors. The reason for this is the importance of identifying two discrete sectors that are of particular importance to London and of relatively less importance to the rest of the UK currently.

These sectors are financial services and the creative & technology sector.

Financial services

The wholesale financial service cluster in the City of London and Canary Wharf (as well as elsewhere in Central London) has built up a global reputation rivalled only by Hong Kong and New York. A fact that is less well-known is the direct dependence of a proportion of the professional service industry in London on the wholesale financial service sector. For the purposes of this report, we have included City lawyers and accountants and other consultants in our wider financial service sector category as their business is driven directly by the City. This enables us to give a more accurate weighting to the sector.

The creative & technology sector

London is home to a large creative & technology sector. The two biggest driving forces of this sector in London are:

- 1) online retail where the UK share is the highest in the world, together with the associated online marketing; and
- 2) fintech – the various digital developments that are changing the world of finance, that are driven largely as an offshoot of the proximity of the London's digital hub and its financial hub.

The categorisation

Therefore, for this analysis we have split the economy into the following categories:

- 1) Financial services and associated professional services (that is the professional services directly dependent on the FS sector).
- 2) Real estate, headquarters and corporate centres
- 3) Creative & technology
- 4) Rest of service sector
- 5) Rest of economy

Table 1 shows the different shapes of the London, UK and rest of UK economies using the breakdown described above.

We see that the two of the industry groupings outlined above, financial services and the creative & technology sector, combined account for around third of the London economy in 2018 GVA terms. For the UK as a whole, that share stands at around half that. Indeed, looking at the UK excluding London, these sectors only account for 12.2% of the economy as opposed to 32.5% of the economy in London. On the other hand, the industrial sectors (essentially construction, manufacturing and utilities) account for only 7.4% of the economy in London (of which the largest part is construction) but 24.3% of the economy for the UK outside London.

Table 1: GVA Shares of the London and UK economies 2018

	London	UK	UK excl. London
Financial services and associated professional services	14.97%	7.08%	4.64%
Real estate, headquarters and corporate centres	19.25%	16.42%	15.55%
Creative & technology	17.57%	9.95%	7.60%
Rest of service sector	40.80%	46.21%	47.88%
Rest of economy	7.41%	20.34%	24.34%

3. Expectations for the UK economy

Figure 1 shows Cebr's expectations for annual GDP growth for the UK economy up to 2025. Our forecasts incorporate the impact of Brexit under the Trade and Cooperation Agreement, with free trade in goods between the UK and EU. Growth expected in 2021 is forecast to be faster than it would have been if tariffs or quotas had been introduced.

Of course, the impacts of the coronavirus pandemic have a large impact on the forecast for GDP between 2020 and 2025. The pandemic has caused a deep recession in 2020, and a significant rebound in economic activity is forecast for 2021 and 2022. However, if the UK had remained inside the EU, the forecasts for GDP in 2021-2025 would have been even higher.

Cebr forecasts 5.1% GDP growth in 2021.

Figure 1: UK GDP growth expectations



Source: Cebr analysis

4. Impact of Brexit under the UK-EU Trade and Cooperation Agreement

4.1. Description

The deal announced on 24th December 2020 between the UK and EU ensures that goods won't face tariffs or quotas. This makes the deal most similar to a 'Canada-plus'-style arrangement, that some had speculated would be a likely outcome of the Brexit negotiations prior to the agreement. However, there are non-tariff barriers which have come into effect, including extra customs checks and forms.

The level playing field agreement ensures that both sides commit to upholding their environmental, labour and tax transparency standards, so they cannot undercut each other. This limits the level of deregulation the UK can undertake in order to increase competitiveness.

Free movement of services has ended, meaning that British businesses have to comply with varying rules across member states. The deal signed at the end of last year made no decision on so-called equivalence, which allows financial firms to sell into the EU single market from the UK. Therefore, 2021 will see more decisions being made in terms of equivalence, which could go in the UK's favour or against. Indeed, the next step is a memorandum of understanding, to be agreed on by end of March, which will agree a framework for EU and UK regulators to talk with each other, but actual decisions around equivalence are expected to take much longer.

Furthermore, automatic recognition of professional standards between the EU and the UK has ended, which means that "doctors, nurses, dentists, pharmacists, vets, engineers or architects must have their qualifications recognized in each member state they wish to practice in," according to the deal. However, the deal does allow for a framework for the recognition of qualifications in the future. There is also no mutual recognition of product standards.

4.2. Impact on migration

The new immigration system, implemented upon the end of the Brexit transition period, is a points-based system. Visas giving the right to work in the UK are awarded to those who meet a specific set of requirements.

4.3. EU contributions

In 2020, the UK continued most of its payments into the EU budget as it also received funding from various EU programmes. The estimated payment by the UK in 2020 was £8.5 billion. Between 2021 and 2028, the UK is expected to pay a total of £19.8 billion, or around £2.5 billion per year on average, £6 billion less per year than was paid in 2020. For the purposes of this modelling, we assume that Greater London pays around a fifth of UK tax.²

² ONS, Country and regional public sector finances: financial year ending 2019

4.4. Effect

Table 2 sets out the initial effects on the London economy of the reduction in trade with the EU from the UK-EU Trade and Cooperation Agreement. It is most closely aligned with expectations for a Canada-plus style agreement that has been analysed in previous Cebr work.³ It shows a potential loss of £9.5 billion at today's prices and level of GDP per year.

Table 2: Impact of Brexit under the UK-EU Trade and Cooperation Agreement

Sector	Share of London GDP (2018)	Impact on EU trade	Impact from labour	Impact from contributions	Impact from deregulation	Impact from new trade	TOTAL per year
Financial services and associated professional services	14.97%	-3.25%	-0.05%	0	0	0	-2189
Real estate, headquarters and corporate centres	19.25%	-1.48%	-0.05%	0	0	0	-1284
Creative & technology	17.57%	-0.30%	-1.05%	0	0	0	-1065
Rest of service sector	40.80%	-1.68%	-1.55%	0	0	0	-5935
Rest of economy	7.41%	-0.55%	-0.05%	0	0	0	-184
Total £ million	£450,278	-£6,979	-£3,772	£1,205	£-	£-	-£9,546

Cebr judges that the deal agreed in December 2020 is close enough to our previous expectations for a Canada-plus style agreement that the impacts on EU trade and the labour market haven't been amended. However, there remains a considerable amount of uncertainty on the impacts of the UK leaving the EU, and the deal agreed upon leaves much undecided. For example, regarding finance, the UK could decide to opt for more deregulation and not be granted equivalence by the EU.

³ Brexit and the Metropolitan Areas: Impact of potential Brexit scenarios on Greater London, Greater Manchester and Greater Bristol, Cebr for LCCI (for the Chambers Alliance). The key assumptions about a Canada-plus agreement made in the report are as follows:

1. Free trade in goods.
2. UK exports have to meet EU standards.
3. UK exports of goods have to comply with additional bureaucratic customs checks, including checks on rules of origin, which could raise costs particularly for those firms with complex supply chains.
4. Regarding services, it is likely that separate agreements could cover parts of financial services trade and possibly telecoms and digital areas as well. We assumed that deals would be made in these areas which would provide about 80% of the market access currently available as an EU member.

