Counting down to Brexit

As the UK’s withdrawal from the European Union draws ever closer, the threat of a no-deal exit has been brought increasingly into focus.

Understand how Brexit has affected operators in the financial services, agricultural, and manufacturing sectors and discover how a no-deal Brexit would impact industries across the economy.
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The Agricultural Sector

Key points

Labour concerns
The weak pound has already led to labour shortages, and agricultural operators have expressed concerns over any disruptions to the ability of UK farms to utilise migrant labour.

Subsidy schemes
Subsidies became immediately larger upon the depreciation of the pound, but whilst existing levels of funding have been guaranteed through 2022, future funding systems have the capacity to cause significant disruption.

Trade
Farming associations such as the National Farmers’ Union have expressed the importance of securing a free-trade deal with the European Union and ensuring that domestic farmers are not overly exposed to international competition following the UK’s exit.

The UK Agricultural sector in a no-deal scenario: summary

A no-deal Brexit has been roundly excoriated by many agricultural spokespeople, with ‘avoiding a no-deal outcome and any short-term political and economic turmoil’ the first of the NFU Council’s six principles on delivering the best outcome from Brexit for British farmers. As many agricultural products are perishable, approximately two-thirds of exports across the sector are destined for the European Union, with the figure rising to 80% for vegetable exports. The tariff and non-tariff barriers brought about by no-deal Brexit would therefore be highly disruptive.

In addition to raising the cost of British exports, significantly reducing their competitiveness, barriers to trade would also affect the availability of farm inputs, such as medicines, and would end the mutual recognition of certifications, affecting the integrity of organic producers. The NFU has also raised concerns that UK producers could be exposed to global competition from cheaper producers operating under different production standards, which would significantly undermine the sector. Barriers to free movement, meanwhile, would cause difficulties over harvest time, and it is uncertain whether proposed immigration changes would allow the flexibility required to prevent disruption. The government has guaranteed funding at the level of the EU’s Common Agricultural Policy (CAP) through 2022, a domestic guarantee that would hold firm even under a no-deal scenario. Ultimately, the consensus in the agricultural sector is that any Brexit deal will require a transitional deal in order to avoid causing significant disruption and difficulties for UK producers.
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Labour

Since the result of the EU referendum, labour concerns have pressed on UK farmers, as migrant labour has been key across the agricultural sector for some time. IBISWorld estimates that 38% of employees on UK farms are seasonal or casual labour, mainly required when seeds are planted in early spring and harvested in the summer, with over 80,000 migrant workers required over the harvest season.

The weakness of the pound following the referendum had an immediate impact on the attractiveness of UK farms as a destination for migrant labour. IBISWorld estimates that the average seasonal labourer earned €412.82 per week prior to the EU referendum. In the following year, however, farm workers earned 13.6% less in euro terms for the same hours, despite improvements in the National Minimum Wage. The lack of motivation for seasonal workers to commit to the same number of hours for effectively less pay due to the depressed pound contributed to 29% of vacancies being left unfilled in the crucial harvest month of September, according to the NFU.

Ensuring access to a competent and reliable workforce is one of the NFU’s key policy aims, with the barriers presented to this by a no-deal Brexit significant. Domestically, there is little desire to work on farms, with a YouGov survey in June 2017, commissioned by the Royal Association of British Dairy Farmers (see IBISWorld report A01.410), finding that less than 5% of UK citizens surveyed would consider working on a dairy farm. A survey by the same body also found approximately 92% of dairy farmers employ EU migrants.

In the government’s recently published White Paper on immigration, the focus was largely on a shift towards a ‘skills-based’ approach, including a consultation on a minimum salary requirement of £30,000 for skilled migrants seeking five-year visas.

Seeds of doubt
Exports as a share of industry revenue

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<tr>
<th>Industry</th>
<th>Exports/Revenue (%)</th>
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<tr>
<td>Poultry Raising</td>
<td>5</td>
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<tr>
<td>Flower &amp; Plant Growing</td>
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<tr>
<td>Vegetable Growing</td>
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<tr>
<td>Sheep Farming</td>
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<tr>
<td>Cereals, Lgs Crops and Oilseed</td>
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<tr>
<td>Forestry &amp; Logging</td>
<td>15</td>
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<tr>
<td>Fruit Growing</td>
<td>25</td>
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However, lower skilled and unskilled migrants would be able to enter the United Kingdom on a 12-month visa, without a job offer, and seek work for up to a year. The NFU has stated that this system would be highly disruptive to businesses that employ non-UK workers on a permanent basis, and that the focus on ‘high-skilled’ immigration does not do enough to address the specific set of skills that are ‘needed for each industry to thrive.’ Most importantly, farming associations highlighted the need for a transitional period, in order for food producing businesses to adapt to any proposed migration changes.

Consequently, there have been a number of calls from the agricultural sector for a new seasonal agricultural workers’ scheme. Indeed, on 6 September 2018, the NFU welcomed the announcement of a pilot scheme to bring 2,500 non-EU workers to UK farms after Brexit. The scheme, which will commence in spring 2019 and run until the end of 2020, will allow non-EU workers to work for up to six months and ease workforce pressures for farmers during peak production periods. However, under the old Seasonal Agricultural Workers Scheme, 21,250 workers were allowed to work on UK farms, illustrating the problems of scale facing post-Brexit labour.

Subsidy schemes: the landscape

Currently, operators in the agricultural sector benefit from the EU’s Common Agricultural Policy (CAP), which provides subsidies through the Basic Payment Scheme. The scheme is intended to act as a safety net for farmers by supplementing their primary income. Producer Organisations, most relevant in the Fruit Growing (IBISWorld report A01.200) and Vegetable Growing (IBISWorld report A01.130) industries, are
also eligible for this scheme. The main qualification to receive payment through the CAP is that operators must actively farm their land, which they do through standard industry-related activities.

These subsidies are an important revenue stream, with many farmers expected to be unprofitable prior to the accounting of subsidy payments. Indeed, according to Farmers’ Weekly, subsidies account for more than 60% of revenue for some farms, whilst Defra estimates indicate that more than one-quarter of dairy farms (see IBISWorld report A01.410) failed to make a profit in 2016-17. Overall, subsidies are estimated to be worth £3.3 billion per year to the UK agricultural sector and, prior to the referendum, the NFU stated that many family-run farms would not be viable without EU funding.

However, the form of the scheme rewards the amount of land farmed, and thereby disproportionately benefits larger operators. Indeed, the top 10% of farming subsidy recipients are expected to receive nearly half of the total payments. This has also pushed up the price of land, placing further pressure on smaller operators. The scheme has come under further criticism for its environmental failings, and Defra secretary Michael Gove’s plans for post-Brexit funding would represent one of the biggest upheavals for British farming in decades.

Whilst much was made in the run-up to the referendum of the importance or the iniquity of CAP payments, the most immediate impact was a sharp increase in the value of subsidies stemming from the depreciation of the pound. As CAP payments are set and distributed in euros, the sharp fall in the value of the pound boosted subsidy earnings considerably: according to Defra the average CAP payment in 2016-17 was £28,000, a 19% increase on the previous year. Ongoing weakness in the sterling meant that CAP payments rose by a further 6% in the following year. Given the pressures on profitability and production faced by many farmers, this was certainly a welcome, if short-term, boost.

**Subsidy schemes: the horizon**

Regardless of how beneficial the short-term effects of Brexit were on the direct value of subsidy payments, it is clear that the longer term poses a number of challenges. The NFU, as part of its Domestic Agricultural Policy, has highlighted productivity, volatility and the environment as the three key factors influencing the UK agricultural sector. As farming investment decisions are generally undertaken over the longer term, prevailing uncertainty regarding the future funding and operating landscapes has already weighed on farmers, and the NFU has stated that it is essential that the government maintains the existing level of investment in farming, as well as providing sufficient time and transition for new policies to be agreed upon and implemented.

Even if there is no deal, the current level of agricultural funding under CAP Pillar 1 is guaranteed through 2020, as part of the UK government’s funding guarantee. The government has also pledged to commit the same cash in total in funds for farm support until the end of the current parliament, expected in 2022, under Pillar 1 and Pillar 2 of the CAP. Whilst a no-deal Brexit would be highly damaging to farms in a number of other ways, funding would be maintained, helping to address farmers’ concerns over Brexit induced volatility.

Proposed post-Brexit funding schemes outlined by Michael Gove would, however, lead to considerable upheaval, in pursuit of one particular key factor of the NFU’s Domestic Agricultural Policy: the environment. Stating that ‘we have an opportunity to deliver a green Brexit’, Gove has announced that, from 2021, a new system rewarding farmers for the public goods they provide will be phased in through 2027, when the last payments based upon the amount of land farmed would be paid. Although the details and levels of the proposed scheme are yet to be elaborated upon, such a change would significantly reduce the level of payments received by the largest operators in the United Kingdom. With efficiency a watchword for both the NFU and Defra, farmers currently operating at a loss and making up the shortfall through CAP payments will have to plan their development carefully if they are to avoid being forced out of operation, as many farms across the sector already have been, in the face of strong competition and consolidation activity. Conversely, as approximately 97% of agricultural enterprises employ fewer than 10 people according to the Office for National Statistics, the shift away from a focus on scale could be highly beneficial to a broader range of agricultural operators.

The proposed new scheme is also expected to address another concern raised by farmers, namely the need to align post-Brexit agricultural policy with the rhythm of the agricultural sector. The stability and certainty offered by the CAP allows farms to plan budgets years in advance, and under the proposed system, the government is expected to avoid setting subsidy payments annually, in favour of longer-term contracts ranging to more than a decade.
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Trade

The depreciation of the pound, in addition to boosting subsidy payments, also had a beneficial effect on the many exporters that make up the UK agricultural sector. As the weak pound made UK produce more competitive on international markets, opportunities abounded, with the Flower and Plant Growing industry (IBISWorld report A01.190) recording a 24% rise in export revenue over 2017-18, for example. The Aquaculture industry (IBISWorld report A03.210) is by far the most export-reliant agricultural industry, with exports making up 60.1% of revenue, but in terms of value it is closely followed by the Cereals, Leguminous Crops and Oilseed Growing industry (IBISWorld report A01.110), at £595.1 million compared with £654 million, although exports for the latter only account for 13.2% of overall revenue. Over the agricultural industries in IBISWorld’s collection as a whole, exports are expected to account for 11.5% of revenue. The export opportunities were therefore valuable and, appropriately, many operators in the sector have been able to make hay.

Whilst the short-term impact of the weak pound has been beneficial, the longer-term impact has been cause for more concern. Farming associations have highlighted the fact that, across the sector, approximately two-thirds of exports are destined for the European Union, and for more perishable goods, the figure is even higher. Approximately 80% of vegetable exports are to EU countries, for example, whilst France alone accounts for more than one-third of exports in the Sheep Farming industry (IBISWorld report A01.450). Consequently, any restrictions to free trade following Brexit would have an immediate negative impact on downstream trading relationships and demand, with export tariffs increasing to an average of 27% on chicken, 46% on lamb, 65% on beef, and range from €172 to €1,494 per tonne in pork, whilst non-tariff barriers would also occasion significant delays. In addition to a range of tariff and non-tariff barriers directly affecting the cross-border flow of agricultural produce, the end of mutual recognition of certification bodies and reduced availability of vital farming inputs, such as medicines and fertilisers, would also affect industry operations.

Although Theresa May’s Draft Withdrawal Agreement was much derided, it did provide important clarity and minimal disruption to the agricultural sector, with a joint statement from Ulster Farmers’ Union, NFU Scotland, NFU England and NFU Cymru stating that: ‘The draft Brexit Withdrawal Agreement, while not perfect, will ensure that there are no hard barriers on the day we leave the European Union, and will allow trade in agricultural goods and UK food and drink to continue throughout the transition period largely as before. This opportunity needs to be taken.’ A no-deal Brexit would clearly cause considerable upheaval and, regardless of the exact form of the future deal, it is apparent that the consensus throughout the agricultural sector is that the maintenance of free trade and the minimisation of non-tariff disruption is highly important, with a transitional deal significant ahead of the UK’s exit. Should an amended form of Theresa May’s Brexit deal pass, many areas of concern would be addressed.

Finally, whilst global free-trade deals could benefit exports, farmers associations have also raised concerns regarding the level of competition the UK agricultural sector could potentially be opened up to, particularly if the UK government opted not to enforce tariffs to prevent a rise in food prices in the event of a no-deal Brexit. New trade deals could open up the sector to competition from countries with lower standards and cheaper products, and the NFU has stated that it is vital that UK farmers are not disadvantaged by future trade deals outside the European Union. One of the most prominent industries exposed to such concerns is the Sheep Farming industry. The Farmers’ Union of Wales
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has opposed a free-trade deal with New Zealand, over concerns that domestic producers would find themselves unable to compete in a system that opens up the United Kingdom to global trade to a greater degree than allowed under the existing EU quota system. Indeed, ‘ensuring that international trade respects domestic production standards’ is a key facet of the NFU’s Brexit policy. Given the significant economies of scale and different welfare standards in other countries, many farms across the agricultural sector would face considerable pressure if exposed to global free trade, with the United States, Australia and New Zealand particularly disruptive to domestic producers.
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The Manufacturing Sector

Key points

Trade
For many manufacturers, the European Union is the single largest market, and the imposition of any barriers to trade would reverse the currently enjoyed benefits of the weaker pound and significantly reduce competitiveness.

Supply chains
Large manufacturing industries have highly international supply chains, with many using just-in-time inventory practices. Non-tariff barriers could render such systems unviable, having a significant knock-on effect throughout the supply chain.

Regulation
Many manufacturers have called for regulatory harmony, stating that seeking to operate under two separate systems domestically and for exports would increase costs and reduce competitiveness.

Divergence, investment and influence
The relocation of the EMA is the most visible example, but many operators across the manufacturing sector have expressed concerns that withdrawing from the European Union decreases the UK’s ability to shape global regulations in its favour, and also makes the country a less attractive location for international investment.

The UK Manufacturing sector in a no-deal scenario: summary

Manufacturing industries heavily engaged in imports and exports will naturally be the most affected, as tariff and non-tariff barriers would affect international competitiveness. Whilst the United Kingdom has remained a member of the European Union, many manufacturers have benefited from the depreciation of the pound, as this has improved the competitiveness of UK products on global markets. Further weakness in the pound stemming from a no-deal Brexit would not have a similar desired effect, however, as the range of tariff and non-tariff barriers would heavily undermine any advantages that could be obtained through a weaker pound. Most manufacturing associations, such as the SMMT, have stated that it is vital the government ‘secures tariff-free access to European and other global markets’. Large manufacturers have repeatedly highlighted the threat that non-tariff barriers pose to their supply chains, with the automotive sector stressing that just-in-time production would ‘grind to a halt’. Although this is a more pressing concern for large and globalised industries, like the automotive and aerospace industries, the effects of delays trickle through their extensive supply chains, and all industries with imported inputs would face additional costs and increased delays to some extent.

Finally, regulatory divergence would pose considerable problems regarding ratification and the legality of cross border trade. This is most apparent in the highly regulated chemicals and pharmaceuticals sectors, with the Department for Business, Energy and Industrial Strategy stating that ‘of all the barriers to trade that we have considered, it is regulatory divergence that causes the most concern for all those from whom we have received evidence.’ Overall, as 60% of industries in the manufacturing sector have a high level of exports, such concerns are highly pertinent.
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Trade

The most apparent effects of Brexit on manufacturers are those regarding import and export trends. As a no-deal Brexit would lead to the imposition of tariffs through World Trade Organisation (WTO) rules, under the General Agreement on Tariffs and Trade, many manufacturers have expressed concerns that their goods would become at a stroke significantly less competitive. Although the EU’s importance as an export destination has fallen over the past decade, an estimated 44% of all UK exports were still destined for EU countries in 2017, by far the UK’s largest export market, demonstrating the weight of free trade in manufacturing considerations. Outside of the European Union, the EU’s average most-favoured nation tariff stood at 2.3% for non-agricultural products in 2013, whilst the average tariff applied by WTO members was 9% in the same year. Given that the United Kingdom could not only lose the benefits of free trade with the European Union, but also any bilateral agreements that the European Union has made with other markets, such as the recently applied Comprehensive Economic and Trade Agreement between the European Union and Canada, which eliminates 98% of tariffs between the two markets, the threat to manufacturing exports is significant.

Nevertheless, the first effect felt was beneficial. The depreciation of the pound made UK exports more competitive overnight. Excluding those industries for which figures are overly distorted by re-export activity, some of the top UK exporters include the Motor Vehicle Manufacturing industry (IBISWorld report C29.100), at £33.5 billion in exports; the Aircraft, Engine and Parts Manufacturing industry (IBISWorld report C30.300), at £30.7 billion; the Measuring, Testing and Navigational Equipment Manufacturing industry (IBISWorld report C26.510), at £8.2 billion; and the Spirit Production industry (IBISWorld report C11.010), at £6.3 billion.

*Some figures are affected by re-export activity

SOURCE: IBISWORLD
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Each of these industries recorded a boost to exports as a result of the depreciation of the pound following the EU referendum. Indeed, the average rate of export growth for industries in the manufacturing sector was 3.8% in 2016-17, compared with an average contraction of 3.5% in the previous year. Whilst the scale of the largest exporters does affect how precisely such figures represent how individual industries felt the depreciation of the pound, it was certainly the case that for many manufacturing industries, the weak pound reversed declining export trends and provided new opportunities, in spite of the increased import costs faced by those firms with international inputs. According to the Scotch Whisky Association, meanwhile, the value of Scotch whisky exports rose by 9% in 2017, representing the strongest growth in six years. More recently, however, prevailing uncertainty has limited the attractiveness of UK suppliers, as international operators worry about future trading relationships. This has had a direct impact on investment in key UK industries, such as those in the automotive sector.

Generally, industries across the manufacturing sector have emphasised the importance of maintaining free access to EU markets. The Motorcycle Manufacturing industry (IBISWorld report C30.910) is perhaps one of the most exposed manufacturing industries, with exports accounting for 68.6% of revenue, and also contains a large number of smaller companies, which are generally more exposed to the imposition of any additional costs due to their narrower revenue bases. In its Position on Brexit statement, the Motorcycle Industry Association (MCIA) has called for the UK’s exit from the European Union to be followed by a ‘stand still’ transitional period of not more than two years, followed by a comprehensive free-trade agreement with the European Union, as well as for the negotiation of free-trade agreements with nations outside the European Union.

Although the importance of exports to the industry makes the response of the MCIA particularly strident, many other manufacturing associations have echoed such concerns. Operators in the automotive and aerospace sectors have raised their voices, with the Society of Motor Manufacturers and Traders (SMMT) suggesting that potential EU tariffs on cars alone could add at least £2.7 billion to imports and £1.8 billion to exports annually, as 56% of industry exports are destined for the European Union. Additionally, with the United Kingdom exporting £3.4 billion worth of components to the European Union each year, it is no surprise that 74.1% of surveyed automotive businesses believed no-deal would damage their business, with half already hit by uncertainty. Ultimately, the SMMT has stated that ‘if the full costs of WTO are reflected in the retail price, an average £15,000 vehicle would cost around £16,500’, posing an incredible challenge to the sector, and proving ‘devastating’ for the competitiveness of manufacturers. Importantly, under a no-deal scenario, it is also highly unlikely that manufacturers would be able to derive benefits from the weakness of the pound, with Aston Martin and Honda both explicitly stating their scepticism regarding this possibility. Instead, the increased cost of imported inputs would be compounded by tariff and non-tariff barriers, further hampering profitability.

Turning to drink, the Wine and Spirit Trade Association (WSTA) has gone further than many other associations, directly urging members to write to their MP, telling them that a no-deal Brexit scenario is unacceptable. With approximately 90% of WSTA members backing the remain campaign prior to the EU referendum, and ties with the European Union strong – 55% of wine consumed in the United Kingdom is imported from the European Union, whilst 45% of spirit exports are destined for EU consumers – it is clear that the threat of a no-deal Brexit has been very much a glass-half-empty situation.

Ultimately the need to, in the words of the SMMT, ‘secure tariff-free access to European and other global markets’ is deemed vital by most manufacturers. In general, the consensus is in favour of a transitional period, to minimise disruption and allow operators to adjust to new and proposed trading regimes. Even if the United Kingdom is able to better exploit trade opportunities across the world following Brexit, improving upon deals made between the European Union and other trading markets, the importance of the European Union as a destination makes securing UK-EU free trade a vital first step. On this note, automotive manufacturers have issued a further warning that barriers to expansion into overseas markets, either for volume manufacturers or premium producers, have not arisen as a result of the UK’s membership of the European Union, but are instead due to economic and geographic factors.

Moreover, trade under WTO rules presents a number of further problems. The House of Commons Library has stated that because the United Kingdom has negotiated as part of the European Union at the WTO, it is likely that it will inherit the EU’s tariff regime upon exit. However, this is not certain, and the United Kingdom may have to establish its own schedules of concessions, such as tariffs and quotas of goods. Deviation from the existing regime could give rise to objections by WTO members, leading to further disruption to trade. Moreover, if the UK government, in an effort to increase free trade and ensure domestic prices do not rise, opts to lower or waive tariffs entirely, operators could face considerable international pressure.
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Component Manufacturing industry (IBISWorld report C26.110) is a useful example illustrative of international threats. The industry has endured considerable volatility, but the protections it enjoyed through EU anti-dumping and anti-competitive import tariffs focusing on photovoltaic material production from China, which only came to an end on 3 September 2018, were vital in allowing the industry to stabilise and, subsequently, benefit from increased competitiveness following the depreciation of the pound. Ultimately, a widespread reduction in tariffs to minimum levels, even if reciprocated, would likely be detrimental to UK manufacturers, as any export opportunities would be outweighed by considerable competitive threats.

Supply chain disruption

One of the key benefits of a transitional deal under which the UK’s trading relationship remains as per the status quo, as highlighted by many businesses, would be the minimisation of disruption to supply chains. This is particularly important for those manufacturing firms that have highly international supply contracts, making use of just-in-time (JIT) production techniques and lean inventory practices. Of these, the Motor Vehicle Manufacturing industry, and auxiliary industries across the automotive sector, and the Aircraft, Engine and Parts Manufacturing industry are perhaps the most prominent. The former is by far the UK’s largest exporter, at £33.5 billion in 2018-19, and also a significant employer, with almost 88,000 staff. These
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two industries serve as useful examples when discussing the impact of a potential no-deal Brexit on UK manufacturers’ supply chains.

In JIT supply chains, which have gathered pace since the 1980s, firms hold little or no inventory stock, with supplies delivered frequently at the point in the manufacturing process that they are required. Lorries arrive at Honda’s Swindon factory every seven minutes, for example, with the warehouses of most manufacturers operating under JIT principles holding only one day’s worth of stock, banking on the reliability of the Dover crossing.

The free movement of goods provided by the UK’s membership of the European Union is a vital framework, without which JIT production would likely grind to a halt, given the scale and length of expected disruptions at UK ports. In a typical UK-manufactured car, 44% of parts are sourced from domestic suppliers, according to the SMMT. Although this figure has risen from the lows recorded in the early 2000s, the threats facing international supply chains are clear. Many foreign parts cross multiple borders, with the practices of some international manufacturers meaning that parts may move in and out of the United Kingdom through the production process.

More than the imposition of a 10% tariff on cars and a 4.5% tariff on car parts, as well as other tariffs across the manufacturing sector, it is non-tariff and customs barriers that would be the most pressing concerns for many UK manufacturers in the event of a no-deal Brexit. Consequently, the response from the sector has been unequivocal. The SMMT has stated that the government’s red lines and conflicting messages were working ‘directly against the interests of the UK automotive sector’. A series of major UK car manufacturers have added their weight to the argument. Honda stated in September that a no-deal Brexit would cost tens of millions of pounds, with every 15 minutes of customs delays costing up to £850,000 per year, and the managing director of Toyota’s Burnaston plant has stated that ‘if Britain crashes out of the European Union...we will see production stops in our factory’, whilst Nissan has described its British operations as ‘a European investment based in the UK’. Most stridently, Ralf Speth, the head of Jaguar Land Rover, has stated that some exposed industries would have ‘no way to survive a hard Brexit’. Meanwhile, when reporting to a parliamentary select committee, the aviation industry warned of turbulence, citing the possibility of a £1.5 billion-per-year headwind if customs and regulatory deals are not made. The concerns raised by such high-flying headline industries are not only concerning for their direct performance, but also for industries in their supply chains. The UK Iron and Steel Manufacturing industry (IBISWorld report C24.100) has already faced a number of challenges affecting its viability, whilst many operators in the highly developed UK electronics sector (see IBISWorld reports C26.110 and C26.120, each with their own supply chain concerns) are intricately linked to the performance of the aerospace and automotive sectors.

On a more direct level, the impact on cash flow for smaller UK manufacturers involved in international supply chains, or supporting industries that are, could be considerable, inducing unwelcome volatility and significantly increasing risk. The international movement of goods under a no-deal scenario would also give rise to direct declarations costs. At £35 per declaration, aerospace supplier GKN has highlighted the considerable impact on costs for larger companies moving tens of thousands of goods. The impact on smaller companies, however, will be proportionally greater as compared with their overall revenue, placing further pressure on the profitability and, in a worst-case scenario, the viability of UK manufacturers engaged in cross-border trade during their production process.

It is therefore unsurprising that the Business Select Committee reported that ‘non-tariff barriers, in the form of border delays and increased bureaucracy, will... affect UK competitiveness’, going on to ‘place a high premium on securing frictionless trade’. Pharmaceutical operators, meanwhile stated that the form of the UK’s exit from the European Union could threaten the
The logistics of supplying the ingredients for more than 12,000 medicines made in the United Kingdom. Although Mrs. May’s Draft Withdrawal Agreement was roundly defeated in the commons, the provisions included therein were cautiously welcomed by many manufacturing firms. Under the proposed two-year transitional period, the trading and regulatory landscape would remain relatively unaffected, ensuring that no friction would arise as the United Kingdom worked to secure a future deal. The SMMT and a number of large motor manufacturers hailed the deal as ‘a welcome first step’, although they continued to make precautions for no-deal Brexit. Given the scale of the defeat in the commons, this was an important contingency, though increasing supply stockpiles will have weighed on margins. Importantly, Airbus stated that ‘if the withdrawal agreement is successful in some form or another then Airbus would consider continuing to invest as the company has done over many years’, highlighting the possibility that any future deal, should it avoid a no-deal situation, would be likely to receive support from large UK manufacturers.

SOURCE: IBISWORLD
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Mitigation

Whilst the progress of government talks is paramount, and largely outside the influence of UK manufacturers, beyond the provision of reports and suggestions, there are some options firms may undertake themselves. The potential ‘reshoring’ of supply chains has been raised and, although this is likely to prove difficult given the highly internationalised system under which many manufacturers operate, with witnesses to the Business Select Committee describing the development of a UK supply chain in time to take advantage of trade deals as ‘a very difficult thing to envisage happening’, a reassessment of supply contracts may be more feasible for smaller and less globalised UK manufacturers. Moreover, firms could take advantage of the Authorised Economic Operator regime and trusted trader status, a scheme highlighted in the automotive sector’s report to the Parliamentary Select Committee.

What is Authorised Economic Operator Status?
The Authorised Economic Operator system is a ‘trusted trader’ programme that aims to enhance international supply chain security and facilitate trade. It is open to all supply-chain actors and was established in the European Union in 2008.

AEO status provides a number of benefits, including: easier admittance to customs simplifications; fewer physical and document-based controls; prior notification in case of selection for physical control; priority treatment if selected for control; and the possibility to request a specific place for customs controls.

AEO operators also receive mutual recognition with third countries and a number of other indirect benefits, such as recognition as a secure and safe business partner.

At the time of writing, only 685 UK companies hold AEO status, with many of these firms being cargo and freight forwarding operators, but the benefits are open across the UK manufacturing sector, from information technology firms such as 3M, to agriculture companies such as AB Agri, and aluminium and cosmetics operators. Nevertheless, the scheme is significantly undersubscribed, with almost ten times more German companies holding AEO status than UK firms. Moreover, higher demand has increased the length of the application process, and a no-deal Brexit would provide a hard check upon the system. In order for manufacturing businesses to fully avail themselves of the means of mitigation, a transitional period is likely to be of paramount importance.

Regulation: chemicals and pharmaceuticals

A further impediment to post-Brexit trade, perhaps illustrated most prominently in the chemical and pharmaceutical sectors, is the problem of regulation and ratification, as well as type approval. Indeed, in addition to emphasising the need for tariff-free access to the European single market, and the avoidance of non-tariff barriers, the Chemical Industries Association (CIA) has highlighted regulatory concerns as a key issue facing the sector, with consistency and continuity the bywords. The UK chemicals sector is currently governed by the EU’s REACH legislation, which allows operators to manufacture, import and trade chemicals within the European Union, and the CIA has stated that UK chemical businesses have spent £550 million registering with REACH laws and communicating safe use of chemical products.
What is REACH?

The EU’s Registration, Evaluation, Authorisation and restriction of Chemicals (REACH) legislation came into force on 1 June 2007. REACH is the key regulation the chemical sector has to comply with in order to manufacture, import and trade chemicals within the European Union, and the regime has a number of key aims:

- To provide a high level of protection of human health and the environment from the use of chemicals.
- To make the people who place chemicals on the market (manufacturers and importers) responsible for understanding and managing the risks associated with their use.
- To allow the free movement of substances on the EU market.
- To enhance innovation in and the competitiveness of the EU chemicals industry.
- To promote the use of alternative methods for the assessment of the hazardous properties of substances.

Under a no-deal Brexit, companies would have to duplicate pre-existing registration duties, with the government stating that ‘companies registered with REACH would no longer be able to sell into the EEA market without transferring their registrations to an EEA-based organisation. Companies would therefore need to take action to preserve their EEA market access.’ This would naturally complicate operations, and the CIA has commented that such a situation ‘will not only weaken our international competitiveness but more importantly, offers nothing more to strengthen health and safety.’ The government has, however, noted that it would intend to ‘grandfather’ REACH registrations into UK law, ensuring that requirements would remain the same, even if legal registration would face more complications.

“In the event of a no deal, the UK would ensure UK legislation replaces EU legislation via the EU Withdrawal Act, establish a UK regulatory framework and build domestic capacity to deliver the functions currently performed by ECHA. The legislation would preserve REACH as far as possible, while making technical changes that would need to be made because the UK has left the EU.”

The concerns of the pharmaceutical sector are similar. The European Medicines Agency (EMA) will physically relocate from London to the Netherlands in early March 2019, and this tangible shift is representative of the shift in agency under a no-deal Brexit. Medical manufacturing is naturally highly regulated, and concerns over batch testing, clinical trials and marketing approvals are paramount. Although the government stated that it would continue to accept batch tests carried out in the European Union, and the Medicines and Healthcare products Regulatory Authority (MHRA) has also confirmed that drug products labelled before Brexit will not require relabelling, the EMA has not officially established how EU and EEA countries will approach medicines batch tested and certified in the United Kingdom following a no-deal Brexit. The implications of this would be significant as, although the MHRA already curates UK-specific marketing authorisation under the existing EMA regime, the EMA has stated that after the United Kingdom has left the European Union all active substances produced in the United Kingdom will be treated as imported products and required to be certified by the MHRA as having manufacturing processes equivalent to the EU’s existing Good Manufacturing Practices (GMP) standards. Finished products manufactured in the United Kingdom would also be required to be subject to batch control testing and batch release from a site within the EEA. Consequently, a report from the Department for Business, Energy and Industrial Strategy has stated that ‘of all the barriers to trade that we have considered, it is regulatory divergence that causes the most concern for all those from whom we have received evidence.’ The report also noted that there was scant evidence of any potential benefits arising from regulatory divergence, with most operators expecting that it would lead to the United Kingdom becoming a less attractive place for investment. Given that planning and development in these sectors generally takes place over a timeframe of many years, the potential for regulatory disruption is a significant red flag.
Counting down to Brexit

Concern over regulatory divergence and the impact this would have on trade has been so heightened that companies have repeatedly increased their stockpiling activity, following government advice. Whilst the six-week stockpile of drugs should ensure that patients do not go without, these are already irrecoverable costs, and stockholdings of goods destined for export are subject to the concerns stated above. Whilst some opportunities may arise for manufacturers, particularly regarding new procedures from the National Institute for Health and Care Excellence that can reduce the time between authorisation and reimbursement, regulatory misalignment would result in a far greater impact on trade than the effects of tariff barriers.

“A deal between the EU and the UK that allows UK companies to continue to be part of the EU REACH system is likely be the only scenario that would not generate additional costs for companies.” - Chemical Industries Association

Regulation: broader implications

Similarly, for the aerospace sector, leaving the European Aviation Safety Agency would be highly problematic, as operators require several certificates for UK-produced parts before they can be sold to EU clients. Under a no-deal Brexit, the United Kingdom would have to reassume responsibility for product certification, which could take years to establish. Aircraft parts, regulated by the Civil Aviation Authority, may currently be used across the European Union. However, as a no-deal Brexit would jeopardise this. Whilst the largest operators in the Aircraft, Engine and Parts Manufacturing industry, such as Airbus and BAE Systems, either do not sell to the European Union or already have facilities for authorisation elsewhere in the European Union, the potential for a hard Brexit has caused more than 200 smaller aerospace manufacturers to apply to come under the jurisdiction of EU regulators.

It has been a similar story for carmakers, as motor vehicles must gain regulatory type approval. The UK’s Vehicle Certification Agency is currently valid across Europe, but in the event of a no-deal Brexit, companies such as Jaguar Land Rover have stated that they may have to apply for type approval outside of the United Kingdom, posing additional costs in both time and money. As it is not possible to hold a certification from two authorities, obtaining type approval from an authority in an EU country would be prerequisite in order to retain access to the single market. Consequently, the SMMT has stated that ‘there are no opportunities for deregulation or divergence’; given the EU’s importance as an export market, as well as the highly interconnected nature of motor vehicle manufacturing, this is unsurprising.

Generally, for large manufacturing industries, it is the case that the UK market is not large enough to warrant a separate set of standards. Whilst some opportunities may arise for those firms with a domestic focus, the general tone from manufacturing industry associations has been one of concern. The CIA has called for all existing REACH registrations to be recognised in the United Kingdom, and has also asserted that it would be better for the United Kingdom to fully remain within REACH and continue to use the services of European Chemicals Agency if possible, rather than setting up (or expanding) separate institutions. Generally, manufacturers have stressed the importance of securing a transition period, minimising regulatory disruption and allowing firms to adapt to any new regulatory landscape gradually. Many of the more internationally integrated industries have set the tone for the future landscape they wish to see, with the SMMT stating that ‘we need to ensure we have a voice in European regulatory policy – helping shape the laws that affect the cars we buy and the cars we build’.

Ultimately, for a sector in which 87 of the 145 industries have a high level of exports, regulatory harmony is of paramount importance, to ensure that their goods are still ratified and accepted in key export markets, of which the European Union is generally the single largest. Beyond barriers to trade and non-tariff disruption to supply chains, the benefits of a more domestically tailored manufacturing policy would be unrealisable should a basic level of regulatory harmony not first be secured.
Counting down to Brexit

The Financial Services Sector

Key points

Passporting
The potential loss of passporting rights under a no-deal scenario would have a significant impact on the globalised financial services sector. Although preparations have been taken, uncertainty has continued to weigh on performance.

Equivalence
Whilst third-country ‘equivalence’ is baked into regimes such as MiFID II, this is not comprehensive, and some operators will have to open branches or subsidiaries in the European Union. Market access based on equivalence was not expanded upon in the Draft Withdrawal Agreement.

Regulation
The Financial Conduct Authority has consistently backed regulatory alignment with the European Union following Brexit.

Economic conditions
A downturn in economic conditions, and an expected fall in the value of the pound following a no-deal Brexit would undercut the demand base for the sector as a whole. However, this could boost the value of the FTSE 100 as the average constituent generates around 70% of its revenue from earnings in a foreign currency. This is likely to increase the value of assets under management of funds that have a high exposure to these shares.

Free movement of labour
Many employees in the sector are EU nationals, and concerns have been raised about staffing barriers.

The UK Financial services sector in a no-deal scenario: summary

The UK financial services sector is highly globalised, and its efficient operations are based upon the free trade of services across the European Union. The loss of passporting rights, under which financial institutions may establish branches across the European Union and trade freely across European borders, is the most prominent concern raised by the sector. More than 40% of UK financial services exports are conducted with the European Union, whilst the Fund Management industry (IBISWorld report K66.300) sourced approximately 40% of its assets under management from overseas clients in 2017. A no-deal Brexit, without provisions for cross-border trading or ratified equivalence, would bring a stop to a large number of operations; insurance industries and the Pension Funding industry (IBISWorld report K65.300), for example, would be placed in ‘legal limbo’, unable to pay out to clients living in EU countries. As a result of this potential check on business activity, 35% of companies monitored in EY’s Financial Services most recent Brexit Tracker confirmed intentions to move some of their operations or staff from the United Kingdom to Europe.

Most industry associations have expressed their desire to retain existing regulatory frameworks, such as Solvency II, as without remaining compliant, UK companies would be unable to access the European single market. The Financial Conduct Authority has consistently backed equivalence and regulatory alignment with the European Union following Brexit, as without these financial markets and consumer protection standards would be closed off. Nevertheless, many have criticised a system of third-country equivalence as lacking in comprehension compared to the UK financial sectors’ current operating conditions.

The economic fallout of a no-deal Brexit would hamper demand from a number of key sectors but, as after the depreciation of the pound following the EU referendum result, could boost the value of the FTSE 100, as the average constituent generates around 70% of its revenue from earnings in a foreign currency. Finally, approximately one in five employees in the City of London are EU nationals, according to the ONS, and potential restrictions on free movement would therefore be particularly piercing for the financial services sector.
Counting down to Brexit

Passporting

One of the most recent and wide-ranging pieces of regulation affecting the financial services sector has been the MiFID II regime, which came into effect in January 2018. The regime aims to make European markets safer, more transparent and more efficient, move a share of trading onto regulated venues, and restore investor confidence. It covers banks, fund managers, exchanges, brokers, pension funds and retail investors, among others. The MiFID II regime includes passporting rights for non-EU investment firms located in nations recognised as providing equivalent supervision. This has increased competition, but non-EU equivalence is likely to be beneficial following the UK’s exit from the European Union, as UK firms will already be undertaking operations to EU standards.

Under the passporting system as set out under the MiFID II regime, firms based in EU member states, as well as non-EU states that are members of the European Economic Area (EEA), can sell their services throughout the European Union. This has made the United Kingdom, with its well-developed London financial services hub, attractive as a base for non-EU firms to establish operations, in order to also access the broader European market. EU business is particularly important for banking and investment activities (see IBISWorld reports K64.191 and K64.301), with the Institute for Fiscal Studies estimating that more than 40% of UK financial services exports are conducted with the European Union. The Fund Management industry (IBISWorld Report K66.300), sourced approximately 40% of its AUM from overseas clients in 2017, with over half of these from clients in the European Union, making the EEA the industry’s largest single client base.

Passporting is perhaps the most notable concern raised by businesses in the financial services sector, as businesses have been reliant on it for their efficient functioning. There are four ways in which a firm may conduct financial services trade with the European Union: Passporting, WTO terms, equivalence or a free-trade agreement. Of the last method, the Comprehensive Economic and Trade Agreement between the European Union and Canada (CETA) is the most recent example. However, financial services operators have raised concerns that CETA provisions fall short of the existing passporting regime, not going much further than provisions under WTO terms. The MiFID II passport and the CRD IV passport are the two most common passporting regimes, although the latter does not provide provisions for third-country firms, and will therefore cease to be an option to UK industries upon the country’s exit from the European Union. Other passporting regimes also apply. In the Private Equity industry (IBISWorld report K64.303), operators may acquire passporting rights through the Alternative Investment Fund Managers Regulations 2013 (for private equity and venture capital funds with Assets Under Management (AUM) of more than €500 million, provided the funds are not leveraged, or €100 million including assets acquired through leverage), or through the European Venture Capital Fund Regulation, which is applicable for funds with less than €500 million in AUM.

Pensions and insurance contracts signed prior to Brexit could be unfulfilled following the UK’s exit. Huw Evans, director-general of the Association of British Insurers has noted that in a no-deal situation, insurers would be placed in ‘legal limbo, where insurers would be unclear if they could legally pay claims for contracts that have been written pre-Brexit, which would have to be paid out in countries in the European Union.’ Should this situation go unresolved, and if insurers do not set up European subsidiaries, or sell existing contracts to EU-based insurers (a process that could take around a year and a half), insurers would be unable to pay out claims for clients in other EU countries, and UK pensioners living in the European Union would not receive their pensions.

What is Equivalence?
The European Commission assesses whether a country’s rules and oversight, the standards of regulation and supervision, are as stringent as its own. This allows the EU to rely on firms’ compliance with their domestic legislation and facilitates cross-border dealings.
Counting down to Brexit

How does Passporting work?
EU member states share regulatory and supervisory standards on financial services. Firms in one member state may apply to their national authority for a range of ‘passports’ indicating that they meet these standards. This allows for the establishment of branches across the European Union, and for free trade of financial services across European borders.

Without a deal, the United Kingdom would become a third country, and UK operators would have to market products on a country-by-country basis, increasing the regulatory burden and compliance costs. Although MiFID II contains provisions for third-country passporting, many operators have raised concerns about a licensing gap. Without a deal, the European Commission would have to decide whether the UK’s supervisory and enforcement regime was sufficient, and only then would accept passport applications from firms individually, in a process that could take a number of months. With the 29 March Brexit Day looming ever closer, and it still being uncertain as to whether a deal may be agreed, and what form it may take, financial services firms have increased their preparations. As of September 2018, 35% of companies monitored in EY’s Financial Services Brexit Tracker had confirmed intentions to move some of their operations or staff from the United Kingdom to other EU countries, up from 19% in the previous year. Even if much of it currently only takes the form of ‘brass plate’ shifting of skeleton staff to set up preparations, such relocation activity is vital; in order to future proof their businesses, financial services firms require a separately authorised subsidiary with sufficient management presence in the European Union to ensure that they could remain ratified and continue trading across the continent. The increased risk of a no-deal Brexit has intensified this activity and, although it is highly unlikely that companies will relocate entirely, contingency plans are in full swing. Contingency planning in the face of the past two years’ uncertainty has already added significant expenses to financial services firms’ cost structures.

Whilst financial services activities conducted in the United Kingdom would not be explicitly affected, the highly interconnected and globalised nature of the financial services sector (17 of the 25 industries in IBISWorld’s Financial and Insurance Activities sector have a high or medium level of globalisation), means that the operations of UK companies are likely to be buffeted by the loss of passporting rights. Private equity firms, for example, rely less on EU passporting rights than other asset managers, but the majority of buyout groups have separate funds that rely more on passporting rights to conduct deals. Moreover, upon a no-deal Brexit, all UK private equity funds will be classified as non-EEA alternative investment fund managers (AIFMs) under the Alternative Investment Fund Managers Regulations 2013. UK AIFMs will have to market on a country-by-country basis using the non-principal private charge, greatly increasing compliance costs and reducing the attractiveness of UK businesses to global clients. The government has taken steps to smooth the process, but this is largely beneficial to foreign firms. The government’s commitment to introducing a Temporary Permissions Regime will allow EEA firms currently passporting into the United Kingdom to continue UK operations for up to three years after Brexit, while they apply for full authorisation from UK regulators. This marks a divergence from general government policy that, under a no-deal scenario, EEA firms would be treated as third-country businesses.

Under a transitional period, passporting rights would remain operational in both directions, providing a smooth transition to any future relationship based on negotiated market access rights. Stakeholders such as the International Regulatory Strategy Group, a practitioner-led body comprising UK figures from the financial and professional services industry, has stated that the fact that the United Kingdom and the European Union will be starting from a shared starting point acts as a strong base for a ‘bold and ambitious’ free-trade agreement. This would be based around three core requirements: market access arrangements; ongoing alignment; and a means for resolving disputes. Market access arrangements are likely to be dependent upon ongoing regulatory alignment, with the equivalence trading regime necessitating regulatory alignment. Many financial services institutions have argued that it is in the interests of both the United Kingdom and the European Union to reach a rapport, with barriers to EU-UK service trade rendering other global financial hubs, such as New York and Singapore, more attractive, to the detriment of both parties. While continued passporting, either after a no-deal or following any transitional period as part of a negotiated exit, is likely to be a panacea, the unique existing alignment between the United Kingdom and the European Union does provide a base for the development of future arrangements.
Counting down to Brexit

Regulation: broader implications

Passporting may be the most prominent regulatory hurdle for a post-Brexit financial services sector, but the rest of the regulatory landscape is no less tumultuous. Financial services operators have collectively spent millions on complying with the latest Europe-wide regulations, requirements for cross-border trading and to safeguard against another financial crisis. Consequently, and in addition to the need for regulatory harmony if operators are to continue their international operations, there is little appetite for divergence. The government has stated its intention that the same rules and laws will apply once the United Kingdom leaves the European Union, as far as possible. In the EU Withdrawal Act it is stated that existing direct EU legislation will be converted into UK law, and existing UK laws that implement EU obligations will also be preserved. Over the longer term, in order for equivalence to remain a viable option, financial services firms will have to continue to comply with a range of EU legislation, although the United Kingdom will lose its ability to influence future regulation from the inside.

The Solvency II Directive codifies and harmonises the EU’s insurance regulation. It was transposed into UK law in January 2016, and is applicable to insurers in the European Union (see IBISWorld reports K65.110, K65.120, K65.124 and K65.200) that have a gross premium income greater than €5 million (approximately £4.3 million). Although opinions about the Solvency directives vary within the UK insurance industry, operators would be unable to access the European single market without remaining compliant, affecting larger firms with cross-border operations significantly. The government has stated that a system of equivalence, whereby the European Commission recognises that a country’s rules and oversight is as comprehensive as its own, is possible in Solvency II. Insurers are also currently subject to the Insurance Distribution Directive, an EU directive that stipulates transparency and minimum

Bully for you
Annual fluctuations in the FTSE 100 index and industry revenue
training requirements of industry operators. Operators undertaking leasing and investment activities must also adhere to the EU Packaged Retail and Insurance-based Investment Products (PRIIPs) Directive. This aims to standardise the information that investment vehicles, including investment trusts, are allowed to provide to investors. Other important pieces of regulation across the sector include the Alternative Investment Fund Managers Regulations 2013, and the European Venture Capital Fund Regulation.

The Financial Conduct Authority has consistently backed equivalence and regulatory alignment with the European Union following Brexit, as without these financial markets and consumer protection standards would be closed off. However, equivalence is not a panacea, and the fact that it is granted unilaterally by the European Union and may be withdrawn with 30-days’ notice provides little in the way of certainty that businesses have demanded. In addition, equivalence is not comprehensive, and instead operates through numerous pieces of legislation. Certain industry operators have expressed dissatisfaction with the position this would leave UK firms in, calling instead for more reciprocal regulatory cooperation agreements. Mrs. May’s Draft Withdrawal Agreement did not go beyond the equivalence regime in its outline for future UK-EU financial services trade. Although equivalence and passporting under MiFID II would remain viable under this or a similar deal, firms would have to make their own arrangements if regulatory regimes are not altered to include third-country equivalence provisions for the UK context.

Wider worries

As the financial services sector is so intimately connected to flux in the wider economy, the shock of a no-deal Brexit could have significant ramifications. The depreciation of the pound has increased overseas earnings of firms with foreign operations, and increased volatility has boosted trading rates. However, economic uncertainty has dampened investment appetite, limiting the amount of cash being channelled into funds. In the Open-Ended Investment Company Activities industry (IBISWorld report K64.304), lower investor risk appetite has caused investors to shift some asset allocation from OEICs (that have a decent proportion of assets invested in equities, which are relatively less liquid) towards other investment vehicles such as strategic bond funds or money market funds that provided high liquidity benefits.

Uncertainty has more greatly affected those financial services industries that are more exposed to the consumer market. Prevailing uncertainty has dampened the housing market considerably, weakening demand for building

![Home sweet home](source: www.ibisworld.co.uk)

**Revenue derived from the residential market**

- Falling residential property transactions indicate a threat to revenue
- 85% Residential Mortgages
- 30% Home loans

**Total Building Society Revenue**

**Total Banking Revenue**

SOURCE: WWW.IBISWORLD.CO.UK
societies and banks (see IBISWorld reports K64.192 and K64.191) for which residential loans account for 85% and 30% of revenue, respectively. Reduced demand for new cars, meanwhile, hit industries such as the Financial Leasing industry (IBISWorld report K64.910), as businesses and consumers postponed purchasing decisions. The Real Estate Investment Trust Activities industry (IBISWorld report K64.306) has been doubly hampered. Not only has reduced consumer confidence lowered spending, compounding worries in the retail market for the industry, but falling property prices have also increased the debt to equity ratio of REITs, and reduced future generation expectations. In general, prevailing uncertainty and the need to undertake spending on mitigation plans has discouraged business investment, weighing on revenue across the financial services sector.

The aftermath of the EU referendum on the wider economy was less severe than initially anticipated. Indeed, the non-residential property market has improved to some extent over the past two years, and increased trading volumes resulting from uncertainty had a beneficial effect on demand for expertise from some industries. However, a no-deal Brexit would be a much sharper shock. With lengthy delays and increased costs on all manner of goods, in addition to a sharp break on trade in services, the consumer and business markets are expected to face a significant check. In addition, a no-deal Brexit would also likely result in a sharp deterioration in the value of the pound. Many banks, businesses and institutions that trade on UK exchanges would be pressured to move more aspects of their operations abroad, with a large number already having taken steps to open offices for regulatory purposes within the European Union. Such inclement financial conditions would also be expected to increase the volume of bad loans, adding a significant element of risk to operations in the financial services sector.

A transitional deal is therefore doubly important for financial services sector firms. Not only do they stand to face exclusion from the regulatory and trading landscape that has facilitated free trade in financial services and barrier-less growth, but the upheaval in key markets resulting from a no-deal Brexit would adversely affect demand and sustainability. As revenue derived from investment income is a hallmark of industries across the sector, downturns in the performance of the stock market, resulting from general economic upheaval, would negatively impact industry cost structures. Although ongoing uncertainty has meant that financial institutions have continued to implement contingency plans, including potential relocation, no-deal is clearly an unwelcome option. Mrs. May’s Brexit deal was met with cautious approval by the banking sector, with TheCityUK (a financial and professional services sector membership body) regarding it as a ‘practical and workable solution’ to the problems facing the financial services sector. Emphasis was placed on the time constraints a no-deal Brexit would cause. Whilst firms have undertaken preparations, prevailing uncertainty has hampered the precision with which steps may be taken, and a grace period, during with greater clarity would be achieved, would provide far less disruption and risk.

A no-deal scenario would lead to considerable uncertainty regarding jobs. The Bank of England has estimated that the United Kingdom is likely to lose 5,000 city jobs by 29 March, a figure supported by the City minister. Moreover, approximately one-fifth of the City of London’s workforce are European nationals, according to the ONS. Whilst the government recently scrapped the planned £65 fee for EU nationals seeking to apply for ‘settled status’, barriers to free movement would limit the efficiency of a sector that relies on its highly mobile and technically skilled workforce.

Ultimately, despite overtures from Paris and Frankfurt, the predominance of London in European finance, and the threat that business could be picked off piecemeal by New York or Singapore should a no-deal Brexit lead to fragmentation, means that a deal is in the interest of many firms across the European Union.
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