

Brexit triggered stockbuilding behaviour by UK businesses in late 2020, followed by a probable contraction in trade in early 2021

The United Kingdom left the European Single Market on 1st January 2021. Its new trade relationship with the European Union is shaped by a free-trade agreement that does not impose customs tariffs but includes non-tariff barriers affecting trade flows of goods. Even after its entry into force, Brexit remains a source of significant uncertainty for many UK businesses. As the deadline of 1st January 2021 approached, imports benefited from stockbuilding effects at the end of the year, in the context of a recovery in Q4. In this respect, French exports to the United Kingdom rose more quickly than to its EU partners. In January, the “high-frequency” port traffic indicator reflected a decline in British foreign trade, probably as a result of the non-tariff barriers introduced at the British border and in reaction to the preceding stockbuilding trend.

The free-trade agreement signed on 24 December 2020 defines the new trading relationship between the United Kingdom and the European Union

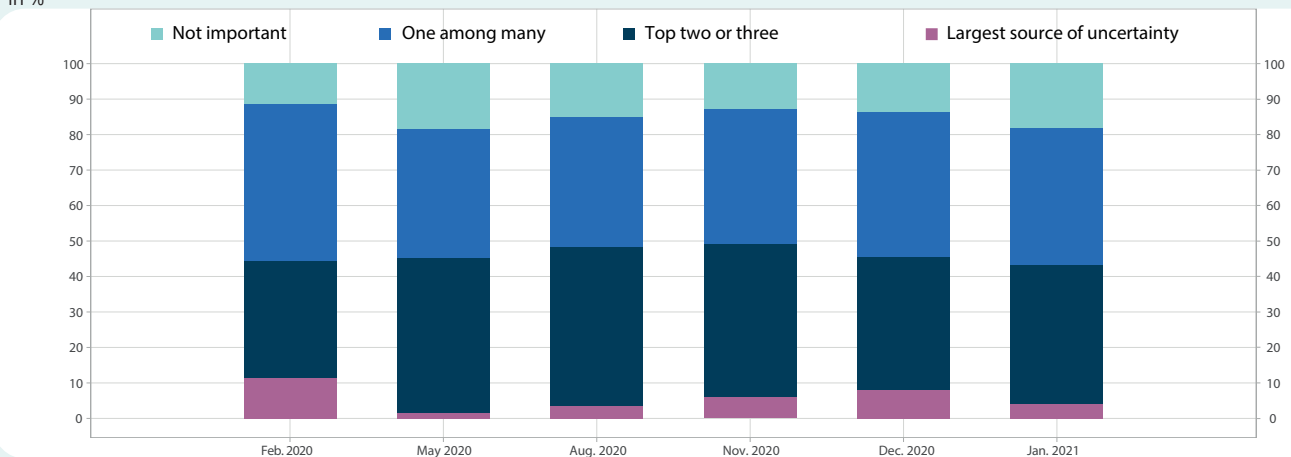
On 1st February 2020, the United Kingdom officially withdrew from the European Union, but retained access to the Single Market during the transition period until 31 December 2020. Negotiations on the nature of the relationship between the UK and the EU led to a trade deal agreed by both sides on 24 December 2020, one week before the deadline.

The agreement reached is a free-trade agreement, which means that there are no quotas or tariffs on the traded goods. However, non-tariff barriers are introduced at the UK border: goods traded between

the EU and the UK are subject to sanitary and phytosanitary inspections, as well as checks on their origin and destination by customs in both directions. These administrative formalities mean additional costs for UK businesses wishing to export to the Single Market and vice versa.

In the short term, the impacts on flows of goods from the EU to the UK should be gradual: UK customs are unilaterally applying transition periods and derogations in order to mitigate problems due to inflexibility at the border. They will not start performing full inspections until July 2021. However, no easing of the administrative burden is envisaged for goods originating from the UK and bound for the EU market. British producers exporting to the EU are therefore subject to all administrative controls.

► 1. In January, more than 40% of UK businesses still saw Brexit as a major source of uncertainty



Note: answers to the question: “How much has the result of the EU referendum affected the level of uncertainty affecting your business?”; only one answer possible.

Source: Bank of England “Decision Maker Panel” survey

International economic outlook

Even after its entry into force, Brexit remains a source of significant uncertainty for UK businesses

The Bank of England’s “Decision Maker Panel” business tendency surveys provide an indication of the degree of uncertainty that Brexit has caused among UK businesses, even before an agreement had been reached (► [figure 1](#)). Between February 2020 and January 2021, the share of businesses that saw Brexit as a major source of uncertainty remained stable at between 40% and 50%. The validation of the free trade agreement does not seem to have dispelled the uncertainty surrounding Brexit at the beginning of the year. However, the proportion of firms indicating that Brexit is the main source of uncertainty has dropped since January 2020 and is now at a very low level, the health crisis also being a significant source of uncertainty.

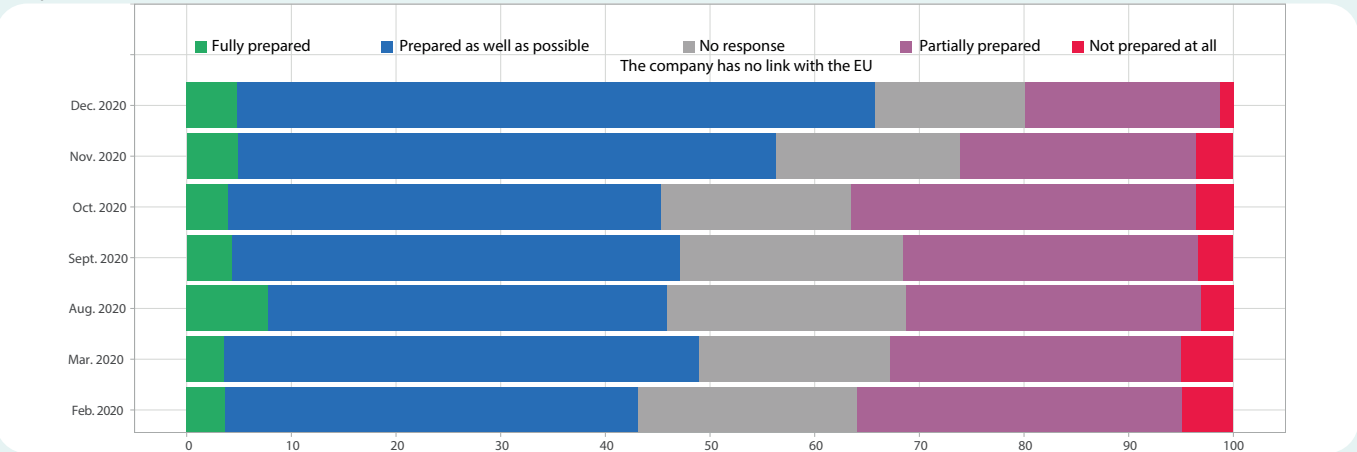
In addition, some of the questions in the Decision Maker Panel concerned the progress made in businesses’ preparations for Brexit. In December, around two in three businesses felt that they had prepared for the withdrawal from the Single Market as best they could – a significant increase compared to previous months and the rest of the year (► [figure 2](#)). However, according to a survey conducted by the British Chamber of Commerce in January, half of all businesses involved in exporting goods to the European Union still reported difficulties in adapting to the changes in procedure.

As before the previous Brexit deadlines, UK imports increased at the end of 2020, benefiting from stockbuilding effects and an economic rebound despite health uncertainties

In Q4 2020, from an accounting standpoint, British growth (+1%) benefited from a 2.2 point contribution made by changes in inventories – one of the highest levels in a decade. Indeed, UK businesses are likely to have been stockbuilding ahead of the withdrawal from the Single Market, as was the case before previous deadlines (March 2019 and October 2019, in particular, see the June 2019 Economic Outlook). According to the Markit surveys, in December, manufacturing companies reported an increase in their inventories (mainly of input products, ► [figure 3](#)). The balance of opinion peaked in December at a level almost matching that of March 2019, the month before the first (ultimately postponed) Brexit deadline.

This stockbuilding behaviour by British businesses boosted British imports at the end of the year. Indeed, in Q4, they rose by 8.9% in volume (after +13.3% in Q3), also benefiting from an increase in domestic demand. Imports of goods grew by 14.2%, reflecting increases in flows from the European Union and from non-European trading partners (► [figure 4](#)).

► 2. At the end of the year, the majority of UK businesses stated that they were prepared for Brexit



Note: answers to the question: “Do you think your business is prepared for the potential extra requirements for trading with the EU once the current transition period comes to an end?”; only one answer possible.
Source: Bank of England “Decision Maker Panel” survey

In France, over the last three months of 2020, exports to the UK increased more than exports to the EU (► **figure 5**). In January, exports to the UK fell, while exports to the EU remained steady, probably as a result of the non-tariff barriers introduced at the UK border in early 2021.

According to the Office for National Statistics (ONS), this increase in imports in Q4 2020 concerned specific products, including health products. The health context is one of the probable explanatory factors, as the production of COVID-19 tests requires specific goods. However, the Brexit context is another important factor. For example, the British government had advised British suppliers of pharmaceutical drugs

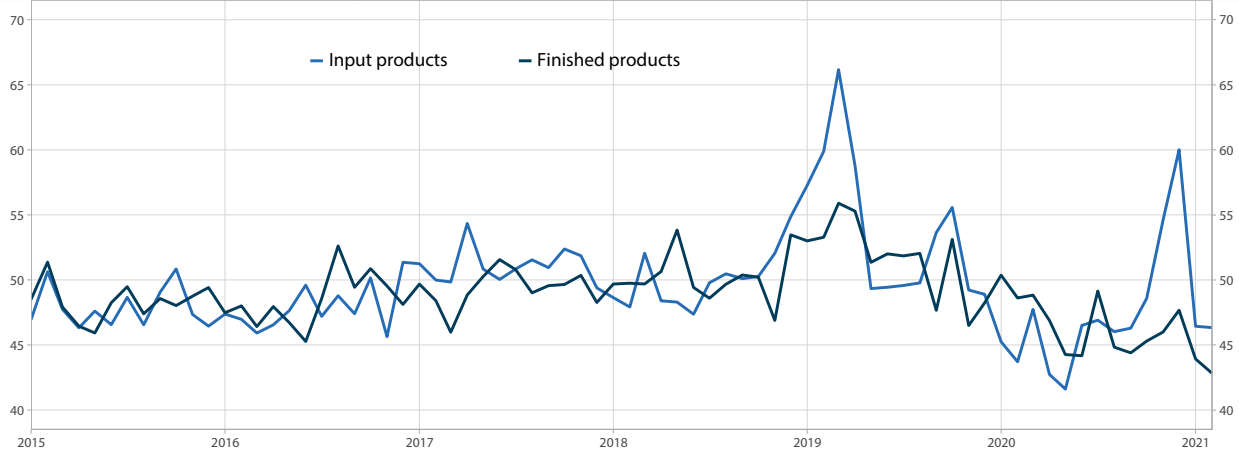
to build up their inventories in anticipation of the increased inspections specific to this type of goods at the border with the European Union. In addition, the ONS reported a marked rise in imports of transport machinery and equipment related to motor vehicle production, again reflecting possible Brexit-related anticipatory behaviour.

The “high-frequency” port traffic indicator suggests a significant drop in UK trade since 1st January

Although UK Customs statistics for January 2021 are not yet available, the UK’s “high-frequency” port traffic indicator reports a significant drop in cargo

► 3. In December 2020, businesses reported a sharp increase in their inventories (especially of input products)

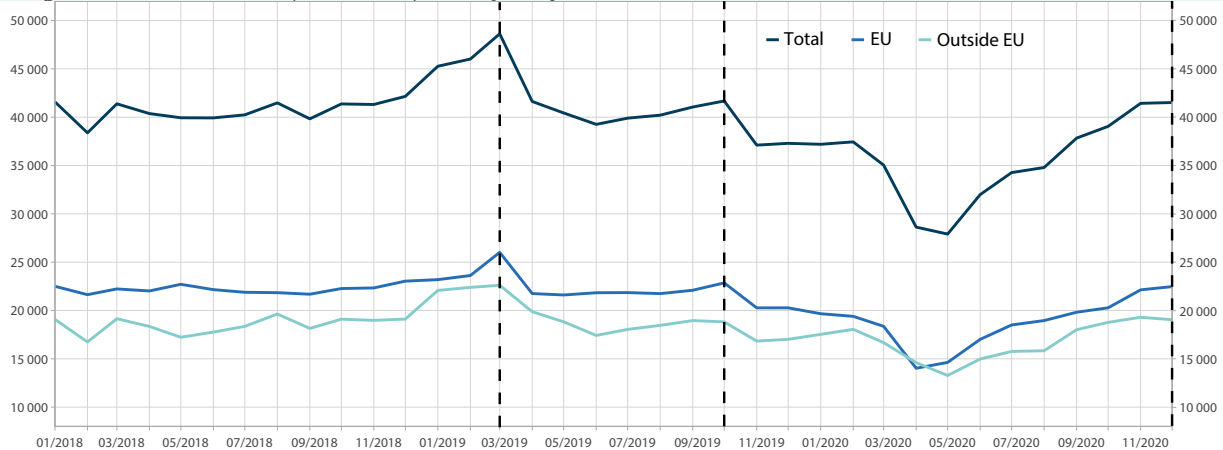
PMI index for inventories in the manufacturing sector (£ M)



Source: IHS Markit

► 4. UK imports rose before Brexit, as they did before previous Brexit deadlines

imports of goods in volume, at chained prices for the previous year, by level (£ M)



Note: the vertical bars represent the months before a Brexit deadline.

Source: ONS

International economic outlook

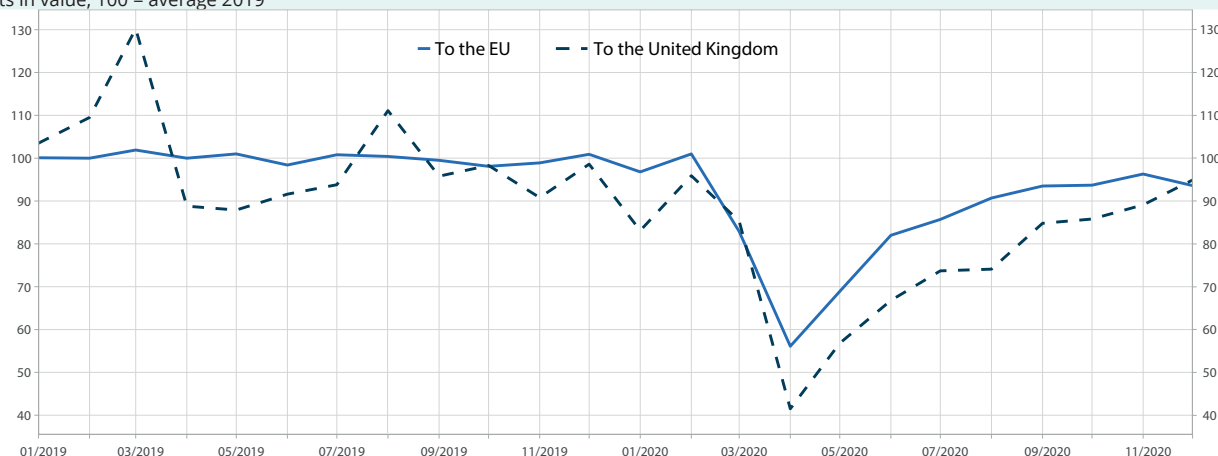
and tanker vessel transits through UK ports since the beginning of the year. During the week of 4-10 January, traffic was 25% lower than during the same week in 2020. Since then, seaborne trade appears to have recovered slightly, but remained below its level recorded one year ago in February, overall.

Furthermore, according to the Bank of England, road vehicle traffic carrying goods around Dover was significantly down on the January figures for the previous three years. These early indicators therefore point towards a likely decline in trade at the UK border at the beginning of the year. ●

David Fath

► 5. French exports probably benefited from stockbuilding trends by British businesses

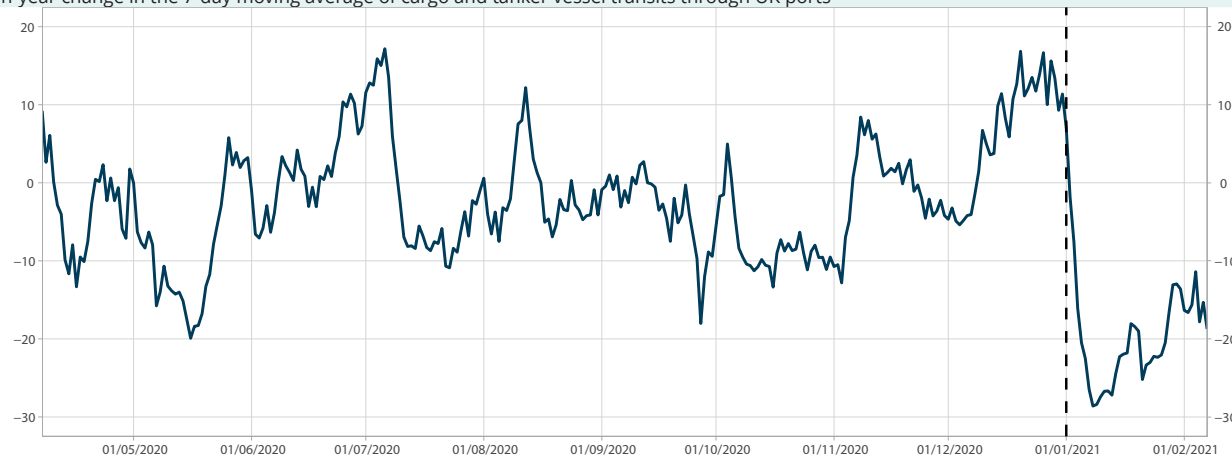
exports in value, 100 = average 2019



Source: French customs

► 6. UK shipping traffic dropped sharply after Brexit entered into force

year-on-year change in the 7-day moving average of cargo and tanker vessel transits through UK ports



Note: the vertical bar represents 1st January 2021, when the Brexit comes into effect. Last point: 28 February.

Source: ONS

Bibliography

British Chambers of Commerce (2021), "Half of UK exporters report difficulties adapting to changes relating to EU-UK trade", February 2021.

Insee (2019) "Planning for Brexit is providing a temporary boost to British imports", *Economic outlook*, June 2019.

ONS (2021), "UK Trade : December 2020", February 2021.

Bank of England (2021), "Monetary Policy Report", February 2021. ●