

BREXIT UNIT

The case for free trade – no ‘ifs’ or ‘buts’

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From 1990 to 2010, free trade helped a billion people lift themselves out of extreme poverty. But the pace of liberalisation has since slowed and protectionism is back in fashion. Fortunately, Brexit provides a golden opportunity for the UK to become a global champion of free trade again. This is potentially a win-win both for the UK and for the rest of the world.

Admittedly, it won't be easy. Powerful lobbies protect the interests of the few who might lose out from a further reduction in trade barriers, rather than the many who would gain. The voices of consumers are rarely heard. Even the economics commentariat is susceptible to fits of ‘ifs’ and ‘buts’. This Briefing addresses some of the main doubts. Further explanation of any of the points is available on request.

The upside, in brief

Leaving the EU will allow the UK to have an independent trade policy for the first time since the 1970s. In practice, this means that the UK will be able to make its own free trade deals with the rest of the world. It may still be several years before these deals can be negotiated and implemented. But in the meantime, the UK will also be able to reduce its own tariff and non-tariff barriers unilaterally.

Brexit will therefore allow the UK to demonstrate the benefits of free trade at a time when protectionism is on the rise elsewhere. Other countries have rapidly opened up their economies before – and thrived as a result. However, they have typically been small and ‘far away’, notably Singapore and New Zealand. In contrast, the UK economy is relatively large and at the centre of the global stage.

EU's relative importance is declining

So what could go wrong? The first objection is usually that any potential benefits from increased trade with the rest of the world could never offset the potential losses from losing unrestricted, tariff-free access to the EU. After all, the EU is the UK's largest single market, accounting for around 44% of the UK's exports of goods and services in 2016.

It is probably unrealistic to expect the UK's future trading relationship with Europe to be as ‘frictionless’ as it is now. Nonetheless, it is in the interests of both sides to agree a new and comprehensive free trade deal that comes pretty close. Even without such a deal, the relative importance of the EU is already declining and set to fall further as the rest of the world, led by the emerging economies, grows more quickly.

Key Points

- Leaving the EU will allow the UK to make its own free trade deals with the rest of the world for the first time since the 1970s.
- The UK will also be able to reduce its own tariff and non-tariff barriers unilaterally, without waiting for other countries to reciprocate.
- The UK can then become a champion of the benefits of free trade at a time when protectionism is on the rise elsewhere.
- More open trade with the rest of the world could also more than offset the loss of trade, if any, with the EU.
- It is probably unrealistic to expect the UK's future trading relationship with Europe to be as ‘frictionless’ as it is now. Nonetheless, a new and comprehensive free trade deal with the EU could come pretty close. In any event, the relative importance of the EU is declining.

Some academic studies have suggested that the UK's exports to the EU could be as much as 60% lower as a result of Brexit. But these studies typically assume that the UK and the EU start again from scratch, rather than the close relationship that now exists following decades of convergence and integration.

Other worst-case scenarios assume that the UK would impose costly tariffs on its own imports from the EU. This also makes little sense. Even in the absence of a transitional deal, the UK would be under no obligation to levy tariffs on imports from the EU. The one important caveat is that it would not be able to treat the EU more favourably than other WTO members. This might mean that some tariffs on imports from the rest of the world have to be cut too. But this would be a net benefit to the UK, not a cost.

The UK is an attractive partner

A second line of attack is that the UK will find it harder to do new trade deals with the rest of the world than if it had simply remained a member of the EU (and, related to this, that it will lose the benefits of the trade deals the EU already has with third countries).

However, the EU still does not have a free trade deal with China, the US, India or Brazil (and only an agreement in principle with Japan). Some argue that it will take the UK longer to conclude its own deals with these countries because they will prioritise negotiations with the much larger EU market. But the UK is still one of the world's largest economies and will surely be nimbler than the 27 nations of the EU trying to negotiate as a bloc.

What's more, there should be some easy wins. Perhaps we cannot rely too much on the US (or joining NAFTA) given the unpredictability of the Trump administration. The Bombardier case is sobering here. But Australia is one of many other countries that seem keen to do a new deal soon.

Of course, closer ties with Australia alone are not going to transform the prospects for the UK economy. But this would get the UK back in the swing of negotiating free trade deals again. More ambitiously, the UK could piggy-back on other agreements. The most promising would be a rebooted Trans-Pacific Partnership (TPP), perhaps as a gateway to an eventual deal with China.

In the meantime, it should be relatively straightforward to replicate – and perhaps improve upon – the trade deals that the UK already has with third countries by virtue of its membership of the EU. Here, Canada is one of several countries that already appears ready to move quickly. After all, these talks would not be starting from scratch.

The case for unilateralism

Even if other countries are not yet ready to sign deals, the UK could still just go it alone. Cutting tariffs on some imports unilaterally would lower costs to UK consumers and increase the amount they have to spend on other things, including home-produced goods and services. To be clear, there would be some losers among UK firms and workers who are exposed to greater competition. These losses are likely to be concentrated and the gains dispersed, which makes this approach politically difficult.

Nonetheless, protecting a relatively small number of jobs in sectors where the UK has no obvious edge is both economically inefficient and unfair on everyone else. There is no shortage of ways to help ease the transition for those adversely affected. There are already too many metaphors involving baked goods in the Brexit debate. But free trade is the best way to increase the size of the pie. The role of government, if any, should be limited to helping share it out.

Finally, there is a lot of nonsense about a 'race to the bottom' and unfavourable jibes about 'Singapore-on-Thames' (an option that actually sounds quite attractive, especially given the huge gains enjoyed by Singaporeans after they embraced free trade). The reality here is that freer trade will allow the UK to concentrate on doing what it does best, activities which are more likely to be higher value and higher paying. The UK has already lost large parts of basic manufacturing to China. Would anyone like to argue that we – or the Chinese – are worse off as a result?

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- Studies suggesting a huge hit to UK trade or GDP from leaving the EU are based on extreme assumptions. It is simply wrong to assume that the UK would be obliged to impose costly tariffs on its imports from the EU. In fact, it would be free to lower tariffs across the board.
- The UK will be an attractive partner for other countries looking to do new trade deals. The UK may be a smaller market than the EU, but it is still one of the world's largest economies. The UK is also likely to take less time to conclude an agreement than 27 nations trying to negotiate as a bloc.
- It should be relatively straightforward to replicate – and perhaps improve upon – the trade deals that the EU already has with third parties. After all, these talks would not be starting from scratch.
- Finally, the UK could always go it alone and lower trade barriers unilaterally. This policy may be politically difficult, but would put the interests of consumers first.