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# Brexit and Outlook for U.S.-UK Trade Agreement

## Introduction

The trade aspects of “Brexit,” the expected withdrawal of the United Kingdom (UK) from the European Union (EU) on March 29, 2019, are of growing interest to Congress. The UK is a major U.S. trade partner, and uncertainty over Brexit presents commercial challenges for the nearly 43,000 U.S. companies exporting to the UK and for U.S. firms operating in the UK, including some 4,000 majority-owned subsidiaries (2016 data). Details about the future UK-EU trade relationship remain largely unknown, and it is uncertain when and to what extent the UK will regain control of its national trade policy—a major objective for Brexit supporters. These factors directly shape prospects for a proposed bilateral U.S.-UK free trade agreement (FTA), supported by the Trump Administration and several Members of Congress.

On October 16, 2018, the Trump Administration notified Congress under Trade Promotion Authority (TPA) of proposed trade agreement negotiations with the UK post-Brexit. The UK cannot formally negotiate or conclude a new agreement until it exits the EU, which has exclusive competence over trade policy and negotiates trade deals on behalf of all EU member states (Fig. 1). In the interim, and absent a U.S.-EU trade agreement, World Trade Organization (WTO) terms govern U.S.-UK trade (like U.S. trade with the rest of the EU), and would apply after Brexit.

**Figure 1. Current UK Trade Status: Fast Facts**

1. EU member since 1973.	
2. Participates in the EU single market, which covers the “four freedoms” of movement of goods, capital, services, and people in the EU (e.g., no tariffs or customs checks). The single market is more developed for goods than services.	
3. Member of the EU customs union, which imposes common external tariffs on non-EU countries.	
4. Part of over 40 EU trade agreements with 70-some countries, as well as ongoing EU trade talks.	
5. Set up a new Department of International Trade in 2016 to rebuild national trade expertise.	

## Trade and Economic Context

The UK, at 15% of the EU gross domestic product (GDP) in 2017, is the EU’s second largest economy after Germany (21%). As a bloc, the EU is the UK’s largest trading partner, while by country, the United States ranks first. Total U.S.-UK two-way trade in merchandise and services (\$236 billion) was about one-third of such UK trade with the EU (\$788 billion) in 2017 (U.S. and WTO trade data).

Many firms operating in the UK are taking steps to reduce trade disruptions post-Brexit, especially if the UK leaves the EU without a negotiated deal, loses its preferential access to the EU market, and returns to trade on WTO terms. While EU tariffs are low overall, WTO terms for UK-EU trade would be significantly different than the

status quo of tariff-free trade. A no-deal Brexit could lead to lengthy customs checks, and some businesses are stockpiling goods to build inventories. UK-EU supply chains, such as for the auto industry, are tightly integrated and with component parts heavily traded. U.S. and other banks are concerned about losing the ability to use their UK bases to access EU markets without establishing legally separate subsidiaries. Some financial institutions, such as Goldman Sachs, J.P. Morgan, Morgan Stanley, and Citigroup, have shifted (or are planning to shift) some jobs and assets from London to other cities, such as Amsterdam, Dublin, Frankfurt, and Paris.

In 2016, after the Brexit referendum, the British pound fell to a record low, and concerns emerged about widespread harm to the UK economy. Doomsday fears may have abated, but prolonged uncertainty over Brexit appears to be a drag on the UK economy. In 2018, the UK economy saw its lowest annual growth rate (1.4%) since 2012. Most analyses predict that the UK economy faces lower growth in all Brexit scenarios, with a “no-deal Brexit” constraining growth rates the most.

## Post-Brexit UK-EU Trade Relationship

Brexit casts great uncertainty over the future UK-EU trade relationship. A draft agreement on the UK’s withdrawal terms and political declaration on the future relationship was rejected by the UK House of Commons in January 2019, and the UK is trying to find a path forward. EU leaders endorsed the deal, which requires approval by the European Parliament.

During the draft deal’s transition period through 2020, the UK could negotiate, but not enter into, its own trade agreements. The UK and EU agreed to work toward a UK-EU FTA, with a fully independent UK trade policy arising after the transition period. As a backstop to address the Irish border issue, however, they agreed to allow the UK to stay in the customs union if they failed to reach an alternative arrangement to avoid a hard border (e.g., customs check, physical infrastructure) between Northern Ireland and Ireland—thereby preserving extensive cross-border economic ties and the peace process. (See CRS Report RL33105, *The United Kingdom: Background, Brexit, and Relations with the United States*, by Derek E. Mix.) Potential scenarios for future UK-EU trade relations have mixed economic and political attractiveness (Fig. 2).

## No Customs Union?

If the UK exits the EU without a deal, it would no longer be a part of the EU customs union and regain control over its national trade policy at once. A no-deal Brexit, whatever its downsides may be, would free the UK to negotiate its own FTAs with the United States and other countries. Likewise, if a Brexit deal emerges where the UK leaves the customs union at some later point (as in the draft deal and political declaration if an alternative arrangement were to be reached

on the Irish border issue), the UK also would be free to negotiate its own trade deals.





In either scenario, the UK likely would seek to negotiate an FTA with the EU, but not be able to achieve single market access. The EU-Canada Comprehensive Economic and Trade Agreement (CETA), for instance, eliminates most tariffs but has major exceptions, such as for services, which are integral to UK trade. Negotiations could be lengthy; CETA negotiations took seven years. Other examples of potential trade arrangements between the EU and non-EU countries are Norway and Switzerland, which are not in the customs union but have tariff-free access to the EU (with some exclusions, e.g., agriculture and fisheries for Norway, some services for Switzerland). At the same time, Norway and Switzerland have no say on EU decisions on rules and regulations and must accept free movement of workers and pay in to the EU budget. Norway's access to the EU market is through its membership in the European Economic Area (EEA). Switzerland (not in the EEA) has more complicated access through over 100 sectoral agreements with the EU.

### Customs Union?

Alternatively, the UK could remain in the customs union or be a part of some other restrictive customs arrangement, and not regain an independent trade policy. This could occur if a UK-EU deal keeps the UK in the customs union permanently or in an extended transition period.

Turkey is a prime example of a non-EU country in a customs union relationship with the EU. Like Norway and Switzerland, Turkey has no voice on EU decisions, but unlike them, does not contribute to the EU budget. Turkey-EU trade is tariff-free on covered products (most goods and processed agricultural products). Turkey has adopted the EU common external tariff, and must apply tariff reductions that the EU negotiates with other countries. To receive reciprocal market access to these EU trading partners, Turkey needs to negotiate its own agreements with them.

**Figure 2. Non-EU Country Arrangements with the EU**

	 Canada	 Norway	 Switz.	 Turkey
<b>EU trade agreement?</b>	FTA	EEA FTA	Many sectoral	Customs union
National trade policy?	Yes	Yes	Yes	No in covered areas
EU market access?	Trade liberalized	SM*	SM*	Goods only*
<b>Pay in EU budget?</b>	No	Yes	Yes	No
<b>Say in EU decisions?</b>	No	No	No	No
<b>Free worker movement?</b>	No	Yes	Yes	No

*Selected examples shown. EEA: European Economic Area; SM=Single Market. \*Some sectoral exclusions.*

**Source:** CRS, based on various sources.

If the UK were to participate in the customs union, it potentially could negotiate on areas outside of the scope of the customs union, e.g., services, digital trade, public procurement, intellectual property, and regulatory cooperation. Still, negotiating flexibility may be limited if a goal of being in the customs union is continued alignment

with the EU. A customs union also could limit UK trade policy such as in applying trade remedies or developing country preference programs.

### Other UK Trade Considerations

The UK, seeking continuity in its trade ties after Brexit, is

- *Negotiating its own WTO “schedule” of commitments on goods, services, and agriculture.* The EU schedule applies to all EU members. Agricultural negotiations are particularly complex as they involve reallocation of EU and UK quotas. The UK's post-Brexit continued participation in the WTO Government Procurement Agreement (GPA) was approved recently.
- *Working to replicate existing EU deals with non-EU countries.* These EU deals would not apply to the UK post-Brexit. The UK has so far concluded a fraction of the deals it aims to replicate. For instance, its bilateral engagement is ongoing with Canada, Japan, and South Korea, which all have trade agreements with the EU.
- *Negotiating sector-specific regulatory agreements.* A focus is on mutual recognition agreements (MRAs) to assure continued acceptance by UK and partner country regulators of certain product testing and inspections by the other. For instance, the United States and UK concluded an MRA on pharmaceuticals, as well as agreements on derivatives and insurance.
- *Taking steps to pursue a range of new trade deals once outside of the EU.* In addition to the United States, potential countries that the UK has identified as of interest for negotiating new trade deals include Australia, China, India, and New Zealand.

### U.S.-UK Trade Agreement Outlook

Should the UK regain an independent trade policy, prospects for a U.S.-UK trade agreement are mixed. Some experts view an FTA as more feasible than a U.S.-EU trade deal, given historical similarities in trade policy approaches and the U.S.-UK “special relationship.” Others caution that domestic sensitivities could impede a “quick win” on a trade deal. Some stakeholders, particularly in the UK, have raised concerns about effects, for instance, on food safety regulations. Key issues also could include financial services, investment, and e-commerce. How U.S.-EU tensions over steel, aluminum, and potential auto tariffs could affect the U.S.-UK negotiations is uncertain.

Each side's approach to the negotiations could be affected by potential U.S.-EU and UK-EU trade negotiations. The United States may be hard-pressed to negotiate with the UK without clarity on the future UK-EU relationship. To the extent that the UK decides to continue aligning its rules and regulations with the EU, its largest trading partner, sticking points in past U.S.-EU trade negotiations (e.g., agriculture) could resurface in the U.S.-UK context.

Congress is expected to continue ongoing consultations with the Administration over the scope of proposed negotiations, and engage in oversight during negotiations. Congress would need to approve implementing legislation for a potential final trade agreement to enter into force. See CRS Report R44817, *U.S.-UK Free Trade Agreement: Prospects and Issues for Congress*, by Shayerah Ilias Akhtar.

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