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‘No-deal’ Brexit would knock 2% off GDP by end-2020

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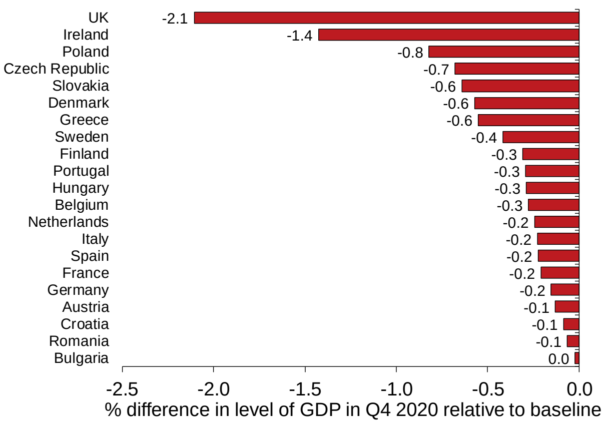
Our modelling suggests that a ‘no-deal’ Brexit would reduce the level of UK GDP at end-2020 by 2.1% compared with our baseline forecast

- **If the two sides fail to finalise a withdrawal agreement and the UK leaves the EU in disorderly fashion in March 2019, it would cause a significant slowdown in the UK economy. Trade would be subject to additional frictions and we would expect to see a substantial sterling depreciation. The impact could be mitigated by looser monetary and fiscal policy, but we would still expect the level of GDP at the end of 2020 to be just over 2% lower than our baseline forecast.**
- If negotiations break down in late-2018, the UK would only have time to re-establish the most critical of the hundreds of international trade and regulatory treaties that it is currently party to via its EU membership. So from March there would be a substantial increase in non-tariff barriers, as well as tariffs being levied on UK-EU trade.
- We would expect financial markets to respond negatively to a ‘no-deal’ scenario, with both sterling and, to a lesser extent, the euro depreciating against the dollar, while equity prices and gilt yields would also be lower than in our baseline forecast. We predict that sterling would depreciate by 10% on a trade-weighted basis by Q2 2019. This would mitigate some of the damage to exports from additional trade frictions. But, combined with the impact of imposing tariffs on imports from the EU, it would push UK inflation above 4% in mid-2019, severely squeezing households.
- We would expect the Bank of England to look through the temporary spike in inflation and cut Bank Rate back to 0.25%. We also assume that the government would divert the funds it had earmarked for the ‘divorce bill’ into higher government consumption and to tolerate the higher borrowing caused by weaker economic growth.
- Looser fiscal and monetary policy should prevent a deeper downturn, but our scenario still sees the level of GDP 2.1% below the baseline (which assumes a deal and a transitional period) at end-2020 and 2.7% lower by 2023. Its close trade links with the UK and heavy reliance on imported goods means the short-term impact on Ireland would be significant, but the impact on the larger Eurozone economies is smaller.

Europe: impact on GDP of 'no-deal' Brexit



Source : Oxford Economics

A ‘no-deal’ Brexit would result in the level of UK GDP being 2.1% below our baseline forecast at the end of 2020. Increased trade frictions would result in much lower exports and imports. Consumer spending and business investment would also be hit, but government consumption would be higher. Ireland would also be hit hard but the impact on larger Eurozone economies would be much more modest.

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