5 January 2021

EU Exit

Purpose of Report

To update members of the implications of the EU Exit as far is it known at the point of writing and the actions being taken to support business.

Thematic Priority

1. Facilitate and proactively support growth amongst existing firms

Freedom of Information and Schedule 12A of the Local Government Act 1972

The paper will be available under the Mayoral Combined Authority Publication Scheme.

Recommendations

Business Growth Board Members:

1. To note the updates on EU Exit
2. To consider what other support the MCA/LEP could offer for businesses in the first few months of 2021

1. Introduction

1.1 The UK will leave the single market and customs union at the end of the transition period on 31 December. Unlike a possible no-deal outcome during the Article 50 process, a Withdrawal Agreement with the EU is now in place and will apply irrespective of the outcome of negotiations. If a trade deal is not in place, UK-EU trade will fall back on to WTO rules. Other elements of the agreement will help avoid an immediate cliff-edge on 31 December 2020 for goods in transit and ongoing judicial processes. Failure to reach an agreement, however, would mean more friction for UK–EU trade.

1.2 At the time of writing, the key dates are:

- 14-17 December 2020: Final European Parliament plenary session of the year. Last opportunity to give consent to the UK-EU agreement.
- 31 December 2020: This is when the transition period established by the Withdrawal Agreement will end.
- 1 January 2021: New agreement on UK-EU relations could enter into force (if an agreement has been reached and ratified by the end of 2020).

1.3 A deal has not yet been agreed – at the time of writing - with only weeks to go until the end of the transition period. If a deal is not agreed in time, the EU and the UK have always said that they would rather go for no-deal than a deal that undermines their interests. It is unlikely that the UK would go back to the negotiating table if there were a no-deal outcome. It is more likely that they will accept the short-term pain and pursue a new route. Both sides would want to avoid the imposition of tariffs, and there is still hope that a deal will be agreed. This is correct at the time of writing; however, this will be revised if significant changes occur between now and publication of this paper, plus a verbal will be given at the meeting.

2. Proposal and justification

2.1 What has been agreed

The Withdrawal Agreement has been in force since 1st February 2020, the day the UK left the EU. It provides for a transition period until 31st December 2020 during which EU law continues to apply to the UK, and the UK remains a part of the EU's single market EU customs union. The transition period stipulated in the Withdrawal Agreement ends on 31 December 2020. It is no longer possible to extend this period.

2.2 What is outstanding

There are three main areas of disagreement that have not yet been resolved, at the time of writing:

- State Aid - the mechanism of giving financial help to businesses
- Fishing - the UK is concerned about who will be allowed to fish in its waters
- Northern Ireland - the EU fears the UK is trying to change an agreement made about the complicated case of Northern Ireland (the only part of the UK to have a land border with the EU)

State aid is financial assistance given by the government to companies that have the potential to distort market competition. If the UK left the EU without a deal, it would no longer formally be bound by the EU's state-aid rules. The EU is concerned the UK could use EU Exit as an opportunity to undermine the single market, by giving its companies an unfair advantage. The UK Government is thought to want a free hand to support companies.

2.3 What will change on 1st January 2021?

Deal or no deal, the end of the year will bring huge changes. With EU Exit changes being phased in, decisions still to be made and the UK-EU relationship likely to change over time, government and business will be thinking about Brexit for a long time yet.

- The UK will no longer make annual payments towards the EU's budget
- People planning to move between the UK and EU to live, work, or retire will no longer be automatically allowed to do so
- The UK will apply a points-based immigration system to EU citizens
- Businesses trading with the EU will face a lot more paperwork

2.4 What matters for the MCA and LEP?

Economic assessment

The Office of Budget Responsibility (OBR) said that a no-deal Brexit could reduce GDP by 2% next year on top of the economic impact of the pandemic. Crucially, this 2% is in addition to the 4% even hit if a deal is agreed. So, the total impact of a no-deal Brexit could be an extra 6% hit on the economy, on top of the pandemic impact. The OBR believes that a no-deal Brexit would shrink the UK's economy and it would remain lower for years to come. This is even more concerning given the economic impact from Covid-19 will deliver a 11.3% contraction in the size of the economy this year. This is the 2nd largest contraction in Europe and the UK's largest for 300 years. Positively, the OBR said it expects a strong recovery from 2021; however, the OECD reported that the UK's recovery would be amongst the slowest globally. Even the worst-case scenario of EU Exit would not result in a short-term hit as severe as Covid-19; however, the pandemic by itself is unlikely to have the same long-term effect on GDP as EU Exit. The OBR reports that the effect of Brexit could be immediate. Impacts could be felt in the first few months of 2021 stemming from border disruption and higher unemployment with a no-deal expected to result in the national unemployment rate rising above 8% next year.

UK Shared Prosperity Fund
In the Spending Review, the Chancellor announced that there will be a pilot for the UK Shared Prosperity Fund (UKSPF) in 2021-22. The UKSPF does not need to be piloted – local areas have been delivering these regeneration funds for decades, and the full replacement of Structural Funds is critical. Positively, the parameters of the scheme align with the Strategic Economic Plan and Renewal Action Plan by focusing upon people, place and employers. Furthermore, it will be targeted at places most in need; however, it says a "portion" of the UKSPF will be based on need. How much of this "portion" is critical for the MCA and LEP.

The UKSPF, in the long-term, will at least match receipts from EU Structural Funds, on average reaching around £1.5 billion per year. This does not take into account the additional funding the UK would have likely received if we had stayed in the EU with extra regions being eligible for increased funding, including South Yorkshire. This could have meant SCR's funding increasing from €110 per head to approximately €500 per head.

Sectors
Any economic disruption from EU Exit will affect different sectors in different ways. Services industries that rely on face-to-face interaction have borne the brunt of the Covid-19 lockdown impacts are inherently less susceptible to higher barriers to overseas trade. The sectors most exposed to EU Exit, especially if a deal is not agreed, are agriculture, manufacturing and finance. Restrictions on trade and labour - i.e. no-deal – will adversely affect manufacturing the most. This means the SCR economy is at increased risk.

Business readiness
Business readiness is the biggest problem for the end of 2020, with the pandemic leaving many firms less prepared than last year. Businesses need to be ready for new trading conditions and to comply with new checks and regulations. The Government's own figures paint a worrying picture of just how few businesses are even aware of the changes coming, let alone prepared for them. As late as October, a third of small businesses believed that the transition period would be extended, despite the deadline for any extension having passed in June. The economic implications of Covid-19 have meant that many businesses do not have the capacity and, more importantly, cash to do what is needed.

2.5 What this means for SCR

Depending on what happens with EU Exit, there is scope to make positive changes to State Aid. The UK Government should consider State Aid as a tool to support the industrial areas and rebalance the economy. It is potentially a key tool of levelling up by strengthening the industrial base of the UK, including SCR. Regional aid is part of State Aid where the public sector can offer private sector investors incentives to locate in less prosperous areas to create or protect jobs. Germany, Italy and France have spent far more on regional aid than the UK. If a deal is agreed, the UK Government should maximise the opportunities this will bring. Or, if the UK set its own rules, there should be an expansion as to where State Aid can reach in order to support more regional areas and how intensely this support is provided. Either way, both options could benefit SCR's economy as it can be used as a means of supporting manufacturing and related sectors.

Places that rely on financial services and manufacturing are most exposed. Leeds is one example. SCR's relatively small financial sector would usually be viewed as a negative, but in this specific situation the area is more insulated. However, South Yorkshire's share of goods exported to the EU is high with 57% of all goods going to this market. This in the top ten out of 40 counties in England. SCR's high share of manufacturing and export of goods to the EU makes it vulnerable to a no-deal EU Exit. South Yorkshire is still a place that makes things. Metals, especially in Sheffield, is still a big part of SCR's high value manufacturing. SCR's share of metals manufacturing dwarfs the national average. Metals is most exposed to EU trade. Positively, Covid-19 has led to a rethink about dependence on other countries for pharmaceuticals, food products, industrial equipment, etc. Reshoring/near-shoring changes presents an opportunity for SCR to capitalise on with more scope for South Yorkshire businesses providing goods that would have previously been imported.

2.6 What we have been doing

Over the past two years the Growth Hub has been providing continual support to businesses with UK transition, but more recently primarily being focused on signposting and ensuring the national resources and information being made available to businesses on the end of the UK transition period are communicated. Since September, specialist UK transition support roles have been provided for businesses in SCR by the Department for International Trade (DIT). However, it is important to state that the uptake and the number of enquiries from businesses on UK transition overall has been very low and this is a pattern replicated nationally through the Growth Hub network and by DIT. The MCA has also been working with local authorities and other local stakeholders on preparing for EU Exit via the South Yorkshire Local Resilience Forum EU Transition Cell. As part of the Renewal Action Plan implementation, a supply chains group has been set up looking at supporting local businesses. This work is not just for Covid-19, it can also assist with disruption caused by EU Exit.

2.7 Proposed work

Government has recently allocated a national funding pot to Growth Hubs to support businesses with UK transition with the SCR allocation being £136k. This process has been somewhat disjointed, and the funding has been issued with restrictive parameters. It is anticipated that this activity will include outreach to businesses across South Yorkshire alongside specialist advice and guidance on both import and export issues and challenges. It is expected at this stage that this activity will be delivered as joint service by the three Chambers of Commerce and a portion for specialist knowledge and support via formal tender process being undertaken on our behalf by West Yorkshire Combined Authority as our regional Growth Hub Cluster lead. This activity sits alongside any existing signposting to national resources and the continued support via the SCR's online EU Resilience tool.

3. Consideration of alternative approaches

3.1 The other option is to do nothing for EU Exit and focus all of our attention on supporting businesses with dealing with and adapting to Covid-19.

4. Implications

4.1 Financial

This report notes that the MCA's most direct exposure to the exit from the EU is around the loss of access to EU structural funding and issues around how state-aid obligations shape our business interventions.

The recent Spending Review provided greater detail on how the structural funds will be replaced by the UK Shared Prosperity Funding, but more detail on how that scheme will be administered is required.

The report notes that the MCA is in receipt of additional funding to resource business support.

4.2 Legal
There are no legal implications associated with this report.

4.3 Risk Management
This approach should mitigate the risk of local businesses with the potential to innovate choosing to relocate outside of the City Region and will ensure the MCA and LEP deliver the SEP and RAP and create stronger, greener and fairer South Yorkshire.

4.4 Equality, Diversity and Social Inclusion
The premise of changing the MCA and LEP's business support, investment and engagement operating model is to create and economy that works for everyone.

5. Communications

5.1 N/A at this stage.

6. Appendices/Annexes

6.1 *NONE*

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Background papers used in the preparation of this report are available for inspection at:

Other sources and references: