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Economic implications of alternative trade relationships: post-Brexit options for the UK

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ABSTRACT – This chapter discuss several key issues for the UK in relation to Brexit. Firstly, how new directions could be initiated to fund infrastructure aimed at boosting the UK's future growth potential and/or promote reindustrialisation by nurturing strategic industries through the early and unknowable stages of their development until they achieve their own international competitive advantage. Secondly, we contest the belief that globalisation has created a new environment eroding the efficiency of traditional policy instruments and with it the relevance of individual nation states. Finally, in this context we conclude by arguing that Brexit offers a unique opportunity to negotiate of a new trade relationship with the EU, together with the rest of the world to both replace previous trade deals concluded by the EU, but also to establish a new set of relationships with a wider set of potential trade partners.

1. Introduction

The project of European integration has been viewed by many as a continuing process of tightening the economic relationships between member states, based upon a common set of institutions and restrictions placed upon national economic autonomy ultimately intended to forge a single European economy. Whenever there is a problem that may impact upon this project, the tendency is to ask how the deepening of economic integration can provide a solution. However, not all European citizens accept this basic premise. Many consider the imposition of constraints upon national governments and parliaments to be illegitimate, whilst that the one-size-fits-all model of European integration, and especially the model surrounding the single European currency, impinges upon the ability of national governments to manage their economies in their own interests. When offered the option of either reaffirming the UK's continued progress towards ever-deeper political and economic integration, or to reassert national self-determination over many areas affecting their lives, UK citizens voted to withdraw from the European Union (EU).

Brexit, therefore, provides the means of escaping constraints imposed by the EU upon the UK's economic development. It allows UK policymakers to design their own regulations for the 94% of UK firms who do not trade with the EU. Further, it releases a significant sum of money that the UK annually transfers to the EU budget that could be used to fund infrastructure aimed at boosting the UK's future growth potential and/or promote reindustrialisation by nurturing strategic industries through the early and unknowable stages of their development until they achieve their own international competitive advantage (Baimbridge, 2016). Additionally, an independent UK has the option of rejecting austerity and stimulating growth rates through a variant of national Keynesianism, by making use of fiscal, monetary and exchange rate policy instruments to prioritise economic growth, low unemployment and low inflation (Baimbridge et al., 2012). Thus, Brexit provides the freedom to develop alternative economic policies that are distinctly different from those pursued across the EU.

One key area where the UK has been consistent in its desire for a closer economic relationship with other EU member states has been in the area of free trade, and this will be a feature of the forthcoming exit negotiations as (hopefully) both sides seek to forge a sustainable future trade relationship that benefits all concerned. Certainly, the UK's trade relationship with the EU will remain important in the short- to medium-term, both for the UK, which currently exports around 40% of its goods and services to the continent, and also for those EU member states who have a substantial trade surplus with the UK. Indeed, as illustrated in Table 1, the UK's very large trade deficit with the EU implies that the UK has been living beyond its means and, since this deficit has continued to rise, it would seem that membership of the EU single market may have exacerbated this structural problem. Brexit offers a potential solution in that the UK would have more flexibility to rebuild its industrial base and seek future trade agreements with the rest of the world, where incidentally, the UK enjoyed a trade surplus of £24 billion in 2014.

Table 1 UK Current Account balance (2014) with selected trade blocs

Regional trade bloc	Current Account (£m)
European Union (EU)	-89,468
European Economic Area (EEA)	-92,261
European Free Trade Association (EFTA)	-1,220
North American Free Trade Agreement (NAFTA)	28,664
Mercosur	1,976
ASEAN Free Trade Area (AFTA)	3,255
Commonwealth (India, Canada, South Africa, Australia)	-2,707

Source: ONS (2015)

This chapter, therefore, seeks to discuss how Brexit may provide a means of escaping constraints imposed by the EU upon the UK’s economic development, before outlining a few of the alternative economic relationships that could be forged between the UK and the EU. These could, for example, include:

(i) The ‘Norway model’, involving participation in the European Economic Area (EEA) to preserve full access to the single internal market (SIM), but at the cost of accepting free movement of capital and labour, the retention of most EU-determined regulation and the UK having to pay EU budgetary contributions;

(ii) The ‘Swiss model’, involving bilateral trade deals, negotiated piece-meal with the EU to gain free trade in goods, but not most services that would still involve accepting free movement of capital and labour, together with (smaller) budgetary contributions

(iii) The 'Canadian model', based upon the negotiation of a free trade agreement with the EU covering goods and some services, but without having to accept free movement or budgetary contributions; or

(iv) The 'World Trade Organisation (WTO) model', where, if a preferential trade agreement cannot be reached with the EU, then trade would automatically revert back to trade based upon WTO 'most favoured nation' rules that would involve trade subject to tariffs.

2. The myth of globalisation and economic interdependence

One of the most influential arguments in favour of continued European integration relates to the assertion that an increased internationalisation, or globalisation, of the world economy has created a new environment which has eroded the efficiency of traditional policy instruments and with it the relevance of individual nation states. This partially derives from conceptions of a 'borderless world' (Ohmae, 1990), within which 'the stateless corporation' operates, relocating the location of production facilities with relative ease on the basis of calculations that optimise profits and productivity (Holstein, 1990; Reich, 1992). Simultaneously, technological advances have produced cost reductions in transport and communications and facilitated the development of a light, information-knowledge-based, service-centred economy (Katz, 1988; Carnoy et al., 1993; Castells, 1996).

This hyper-globalisation thesis suggests that the integration of financial markets, the free movement of capital, the rising importance of Trans-National Corporations (TNCs) in global manufacturing production, and their use of Foreign Direct Investment (FDI) to expand their control into an increasing number of national markets, has undermined the abilities of nation states to successfully manage their own affairs (Ohmae, 1990; 1993; 1995; Reich, 1992; Hay, 1999). Hence, the authority of national governments has 'leaked away, upwards, sideways, and downwards', with states being 'hollowed out' by a combination of ease of evasion of regulation and dramatic increases in capital mobility (Cerny, 1990; Strange, 2000). As a result, advocates for European integration suggest that it can provide a bulwark against the worst effects produced by these global forces (McGrew and Lewis, 1992).

The problem with this thesis is that globalisation is quite possibly "the most contested concept in contemporary social science" (Grant, 2002:41), being "invariably over-used and under-specified” (Higgott and Payne, 2000:ix). Indeed, Wiseman (1998:1) has been prompted to identify it as “the most slippery, dangerous and important buzzword” of modern economic discourse. Certainly, the cost of communications and transportation of goods has declined substantially over the past half a century (Rustin, 2001:18), facilitating pan-national supply chains and an expansion of international trade exceeding global growth rates (OECD, 1996:9), whilst FDI has enabled TNCs to gain dominance in many global markets (Ruigrok and Van Tulder, 1995). Yet, the clearest evidence of globalisation does not derive from trade, but rather the spectacular increase in short-term financial capital flows and speculation. Whereas in 1971, 90% of all financial transactions were made to facilitate international trade and long-term productive investment (Eatwell, 1995; Watson, 2002), trading on the major foreign exchange markets today are around one hundred times greater than the equivalent value of international trade and dwarfing the total world expenditure on crude oil (Eatwell, 2000; Helleiner, 2000). Indeed, one estimate suggests that derivatives trading alone accounts for more than twelve times global GDP (Castells, 2000).

Yet despite these dramatic changes, there is little convincing evidence to indicate that globalisation has undermined the efficiency of institutional frameworks within which economic policy operates (Garrett, 1995; Scholte, 2000; Whyman, 2007). Careful examination of the data leads a number of theorists to conclude that contemporary phenomenon relates more closely to internationalisation than globalisation (Hirst and Thompson, 1996; Wade, 1996). Indeed, it is perhaps worth noting that claims of ‘the end of the nation state’ have coincided with more nation states existing than during any previous historical period of world history. National macroeconomics remains a viable alternative for any nation to pursue (Baker et al, 2002). Nation states remain essentially sovereign; influenced by the international economy, certainly, and with their freedom of movement constrained by the consequences of specific actions, naturally, yet remaining sufficiently autonomous to devise and implement a distinctive, self-determined economic strategy tailored to the needs of its economy and preferences of its electorate.

Given the continued viability of national economic self-determinism, the question turns to the selection of the type of economic strategy that best meets the objectives of the individual nation. This could, for example, draw inspiration from the low tax, deregulated, neo-liberal market-orientated economics, as hinted at in UK Prime Minister May’s recent speech on her perceived options for Brexit[1], or alternatively it could embody a more interventionist, active macroeconomic policy evolving from Keynesian principles. Whatever option is selected, this will be based upon the democratic will of the UK citizenry, expressed through its election of representatives to the House of Commons and thereby the formation of the national government, rather than being stymied by the over-exaggerated claims of the hyper-globalists that would dismiss the relevance of any such discourse. It is this that motivated the expression of electoral will that resulted in Brexit and it is to consideration of alternative aspects of national economic policy in relation to new trade relationships open to the UK post-Brexit that we now turn.

3. Alternative trade relationships: within the European sphere

There are various options that the UK could choose, including:

3.1 Norway model

This strategy would involve the UK formally withdrawing from the EU and re-joining the European Free Trade Association (EFTA) that it helped found four decades ago. In the process, the UK would be eligible for membership of the European Economic Area (EEA). Article 41 of the convention establishing EFTA states that any state may accede provided it receives the approval of the EFTA Council, or alternatively the Council may negotiate bilateral agreements with individual states subject to its unanimous approval by all member states. Article 42 establishes the right to withdraw from the convention after 12 months advance notice. Similarly, Article 128 of the EEA Agreement states that any European state becoming a member of EFTA can apply to the EEA Council to be party to the agreement, with the terms and conditions subject to negotiation. All future EU members are required to apply to become party to the agreement.

The EEA is an agreement made between EFTA (less Switzerland) to extend the internal market of the EU and that of the EFTA participants to create a trading area of 28 countries and some 462 million people. This is the world's largest and most comprehensive multinational trading area that came into force on 1 January 1994. Under the agreement, there is free movement of goods, services and capital across the entire area, whilst Article 28 provides for the free movement of persons and a single labour market across all member countries. Participants are encouraged to co-operate in the fields of environmental protection, social policy, education and research and development programmes. Exceptions to coverage include agriculture and fisheries, whilst the EEA has no common external tariff and therefore requires the identification of country of origin for all goods and services.

As a member of the EEA, the UK would possess full access to the SIM and retain some influence over the rules that affect trade with EU nations. The EEA ensures free trade without the discrimination against external nations created by a customs union. The terms of the EEA stipulate that the UK business sector would operate under the same general conditions as its EU competitors, whilst ensuring that EEA member states develop relevant legislation jointly without the EU imposing standards arbitrarily. The EEA provides member states with the right to oppose and veto EU law if they feel that it operates against their national interest. It also offers the possibility to participate in EU research projects and co-operation on the environment and the social dimension of EU legislation should any EEA participants find these beneficial.

A net transfer of income to the EU budget is part of the requirement for EEA membership, but it would be significantly lower than the high budgetary burden imposed by full EU membership upon UK taxpayers. Taking into account differences in per capita GDP compared to Norway, the UK's fiscal contribution might be anticipated to be around 0.2% of UK GDP, which is around 40% of the UK's current net contributions to the EU budget. Membership of the EEA also releases the UK from pressure to participate in the ERM, stipulated by the TEU. Given the UK's previous unfortunate experience of ERM membership, and the still larger disadvantages it would suffer through participation in EMU, this constitutes a significant advantage. Thus, the EEA provides many of the advantages of EU membership without some of the costs.

Norway can also be used as a political precedent since their electorate rejected EU membership in a national referendum and yet was able to participate in the EU single market by means of the EEA. The EU have not sought to 'punish' Norway for failing to persuade its people to become full members, and on the contrary appear eager to take advantage of their addition to the single market to export goods and services, whilst having Norway pay a contribution towards the EU bureaucracy that manages the market.

An advantage is that EFTA is a similar type of trade agreement to NAFTA in that it does not impose undue costs and restrictions upon member governments, barring those minimum rules necessary to maintain the effectiveness of the free trade area. The only significant differences are that the EEA is not as explicit on the issues of intellectual property and foreign investment, whilst it progressively adopts updated rules on trade harmonisation once these are agreed between the EU and EFTA members. Thus, UK membership of the EEA and NAFTA could establish closer co-operation between the two trade blocks around a two very similar free trade agreements.

The main disadvantage of the EEA involves participants having to accept EU-determined rules and regulations relating to SIM trade with little effective input. In effect, EEA members become 'rule takers' rather than, as full EU members, they are 'rule makers'. This difference can be over-emphasised, of course, since the UK is currently one of 28 member states and therefore can only influence the drafting of new rules and regulations through argument and/or building effective majority alliances with other members. Nevertheless, as an EEA member, the UK would have less ability to shape the trade rules within which it would have to operate. It is possible that, with the UK joining the existing EEA members, this might reduce the power imbalance with the EU somewhat, and facilitate greater partnership rather than subservience between EFTA and the EU, however, there have been no such proposals made in this direction to date.

Partly as a result of the lack of influence over rules governing its own industries and trade, the Norwegian government has expressed a degree of dissatisfaction with aspects of the operation of the EEA. It has, furthermore, welcomed the free movement of labour as a means of resolving what had become persistent skill shortages within its economy, and yet the Norwegian government had registered its concern that free movement simultaneously undermines high quality working conditions and can lead to social dumping (NOU, 2012). In addition, SIM rules would stifle independent policymaking (Baimbridge et al., 2010; Swidlicki et al., 2016).

3.2 Swiss model

One further option that the British government could consider relates to formal withdrawal from full EU membership and its replacement with a bilateral trade agreement between the

EU and UK. It is sometimes referred to as the "Swiss position" as, following rejection of EU membership by a majority of its citizens and cantons voted against EEA membership in December 1992, Switzerland negotiated a series of over 100 bilateral treaties with the EU, including a 1972 Free Trade Agreement, which covers industrial goods (Church 1993).

Since the UK is ill served by participating in the CAP and the CFP, a restriction of free trade with EU nations to industrial and financial goods and services would prove more beneficial than the present status quo. The remaining EFTA countries negotiated such a free trade agreement with the EU in 1972, after the UK, Denmark and Ireland had joined the EU, thus escaping from the financial burdens and policy constraints imposed by EU membership. As with membership of the EEA, this approach would allow the UK to re-orientate its economic policy to serve its own perceived national interest rather than those of competitor EU countries. The money saved by non-contribution to the EU budget could be used to increase incentives for productive investment within the UK, and for state expenditure on infrastructural and research-based projects that increase long-term competitiveness. This option provides greater freedom than EEA membership.

These decisions did not haemorrhage economic vitality; instead they strengthened the Swiss economy. Amongst OECD countries, agriculture apart, there is no economy more open to the outside world than Switzerland. Exposure to such competitive pressures encouraged the development of some of the world's most international-orientated companies. Switzerland is the fourteenth trading nation in the world and the second trade partner with the EU (after the USA) and the third supplier after the USA and Japan. Switzerland has managed to maintain relatively low levels of inflation, interest rates and unemployment, together with a significant balance of payments surplus, particularly when compared to the larger continental EU member states. Thus Switzerland is benefiting from its arm's-length relations, despite a continued eagerness amongst its political elite for future EU membership. Consequently non-membership of the EU has failed to hamper its economic development or its trading potential.

Despite economic success outside the EU, the Swiss authorities express two fears, which are familiar to UK citizens when confronted with the possibility of a change in relations with the EU. First, since the majority of trade is done with EU nations, membership may prove essential to protect it. Second, absence from the EEA may result in EU discrimination against Swiss-made goods through technical barriers. These concerns may be over-exaggerated. For example, in the Swiss case only 58% of exports and 71.5% of imports relate to the EU, so that its economy is less orientated towards the EU than most commentators claim. Additionally, like the UK, an increasing proportion of its international trade is being conducted with the fast growth areas in Asia and the USA rather than with the slow-growing EU. Thus Switzerland's dependence upon the EU market is likely to diminish in the future. The trend would be accelerated if the UK, Switzerland's fifth most important trading partner, left the EU.

In answer to the second point, the EU nations benefit far more than Switzerland from their trade so that they are unlikely to engage in discriminatory practices that could endanger their own more sizeable exports. Moreover, the Uruguay GATT (latterly WTO) agreement prevents arbitrary treatment of a nation's exports in any market, thus preventing active discrimination against Swiss, or any other countries', exports by the EU. Of course unofficial barriers to trade do exist, but EU membership is no guarantee that these will be dismantled.

The Swiss option does involve acceptance of the free movement of capital and labour, and the latter has created difficulties for this relationship with the EU. For example, a 2014 referendum decision instructed the Swiss government to introduce immigration quotas, which would have terminated the bilateral relationship with the EU had the Swiss government not decided to effectively side-line the referendum result in favour of less drastic policies intended to curb the impact of migration rather than placing restrictions upon the inward flow. This experience raises difficult questions for the UK, should the government seek to pursue the 'Swiss option', since regaining some measure of control over immigration was a key issue in the UK European referendum (Booth et al., 2015).

The 'Swiss option', therefore, provides a more flexibly means of securing a close relationship between the EU and the UK, but the insistence upon acceptance of the free movement of capital and labour is likely to prove to be difficult, if not impossible, for the UK to accept, as it goes against the expressed democratic will of its people.

4. Alternative trade relationships: a global vision

Successive British governments have sought to place the UK at 'the heart of Europe' and in the process have accepted the idea of the inevitability of a drift towards broader and deeper economic and political integration across a large swathe of the European continent. This is not to say that leading British political figures have not made personal stances against this process, together with a larger number who have argued for a loosening of the constraints imposed upon nation states by the integration process (Abbott, 2000; Redwood, 2000; Benn, 2006; Gould, 2006; Mitchell, 2006; Owen, 2006; Shore, 2006). Moreover, both Conservative and Labour governments have drawn their 'red lines' or vetoed specific new initiatives usually seeking to limit national self-determination. However, notwithstanding these efforts, the process of ever-closer unification has progressed from the trade-related common market, through the creation of a SIM, to the establishment of EMU.

Withdrawal from the EU provides one means of escaping these increasing constraints imposed by the EU upon the UK's economic behaviour, and which are not fully eliminated by those options involving retained EU membership. Renegotiation could reduce many of these direct costs, but would be exceptionally difficult because a gain for the UK would involve a net cost for other member states. The Swiss option is the most palatable, but if this is achieved with the UK remaining bound by the Treaty of Rome then economic policy remains fundamentally constrained and speculators could therefore 'punish' Sterling for non-compliance with EMU rules. Therefore, in view of the varying but substantial costs implied by any form of EU membership, a further option for the UK is complete withdrawal, so that it can repatriate the ability to employ those policy tools it sees fit to better manage the country in its natural interests.

Once attained, the UK is free to operate any economic policy it wishes. It could take the form of a determined effort to rebuild large sections of the UK's industrial base, decimated by EU, and accelerated by ERM, membership. Burkitt et al. (1997) outlined the essential elements of one such strategy. It could pursue a low-tax, market-orientated strategy, or else seek to stimulate growth rates through a combination of national Keynesianism, an active labour market and industrial policy. However, the crucial point is that UK citizens would possess the power to decide how they are governed and how the economy is run, rather than exercising merely a token vote at election time because important decisions concerning fiscal, monetary, exchange rate and trade policy are taken in Brussels. The economy would be free to react to external shocks in a way that suited its particular circumstances, not what suited Germany as the strongest EU state, or the 'average' member state, whether or not such a creation of statistical indexes actually exists! Indeed, as the German and Japanese economic 'miracles' were partially based upon a competitive currency and long-term low interest rates for industrial finance, the UK could adopt a similar approach to compete more successfully with EU members rather than be restricted by EU economic policies that are not in its interest.

The argument that the UK can only exercise any influence on world events within the EU is perverse, appearing to be simultaneously defeatist yet hankering for a world leadership role. The UK lost its former dominant world position because of economic problems. Decades of slow economic growth reduced the UK from being the leading world economy before the turn of the century to a medium sized economy in the 1990s, with political power declining accordingly. Japan and Germany obtained increased international influence not because of foreign policy or military might, but because their economic strength compels attention. If the UK is to regain influence, it must be based upon economic success, which is less likely to be secured within the monetarist-inspired EU-EMU policy straitjacket. Furthermore, the UK could secure international influence far in excess of its size through less conventional means. The Scandinavian countries, for example, achieved significant prestige for their environmental and human rights campaigns. The UK, when it established the National Health Service, was likewise a model that countless other countries used when constructing their own welfare systems. Likewise, the British democratic system is still admired by many sections of the globe as the 'mother of parliaments'. International influence does not, therefore, have to be of the traditional type. Even the latter can be more effectively attained through UK participation in the G7 summits than by being one voice amongst 28 (or more) within the EU.

The belief that withdrawal would reduce the flow of foreign investment into the UK is widely held, but a UK economy growing faster outside the EU with a permanently competitive exchange rate may prove to be equally attractive to foreign investors. Foreign-based companies locate productive facilities in the UK to enhance their profits through producing output it can sell in the British and European markets, utilising the skills and abilities of a well-educated and flexible labour force. If firms remain profitable irrespective of British membership of the EU, they will continue to invest in the British economy in large numbers, as they currently do with few indications that the UK will participate in the most visible extension of European economic integration, namely the single currency.

Nor is the idea that withdrawal from the EU would provoke retaliation from current EU 'partners' any more probable. It is likely that EU negotiators will impart political pressure upon the UK, either to seek to persuade the UK to reverse its decision to withdraw or else to persuade those amongst the citizenry in other EU member states that withdrawal is not an attractive proposition. Nevertheless, this rhetoric will be tempered by the fact that the erection of any significant trade barriers between the EU and the UK will harm EU member states, given their large trade surplus with the UK and their reliance upon continued access to inexpensive capital through the City of London. It may also prove counter-productive in the medium term because any such restrictions placed upon trade with the EU would encourage the UK to complete a more rapid and substantial reorientation of its trade towards global markets, sourcing goods and services from outside of Europe, and accelerating its programmes to rebuild UK industrial capacity and to ensure the continued international competitiveness of its produce. Were this successful, it would create the very example of a successful Brexit that might prove attractive to those EU citizens who find the current model of European integration unappealing. The EU negotiators, in pursuing a hard line in their negotiations, would in effect have scored an own goal.

4.1 Canadian model

Withdrawal from the EU is only a first, necessary step. Once achieved, the UK can develop whatever trading relations with other nations. It may, for example, seek to negotiate a Free Trade Agreement (FTA) with various Commonwealth nations. Indeed, the Prime Ministers of Australia and New Zealand have already expressed their interest in pursuing such an agreement. In addition, the new US administration has stated its interest in negotiating a FTA with the UK. Given this likely *modus operandi* for the UK to pursue free trade with multiple partners, the negotiation of a FTA with the EU would, therefore, seem to be an obvious choice for a future trade relationship between the two parties. Depending upon the scope of the agreement, it would extend free trade between the UK and the EU to goods and some services, but excluding agricultural products. It would secure continued free trade between the UK and EU member states without the necessity of insisting upon continued budgetary contributions, the harmonisation of regulations, the acceptance of free movement of capital and people, and the unwelcome (to the British people) pretensions of economic and political union.

One possible starting point for negotiations could be the FTA recently completed between Canada and the EU, although it is likely that the UK would seek to add financial services to the existing Canadian agreement. This might not prove to be an insurmountable obstacle, given EU industry's reliance upon the continued access to inexpensive capital through Europe's premier financial centre, based in London, and the likely financial instability that may be caused if this link were to be broken.

A FTA would require 'rule of origin' regulations, which is where a UK company exporting into the EU Single Market would have to state the proportion of the value of the good or service which originated in the UK. The reason is to prevent UK companies acting as re-importers of finished goods from elsewhere into the Single Market, and thereby evading the Common EU tariff. This does add a minor cost to UK exporters, estimated at between 2-7% of the value of the goods traded (Cadot et al., 2006), yet it would enable the UK to achieve free trade in goods, and possibly some services, without having to accept additional elements of political and social integration (Milne, 2004).

4.2 World Trade Organisation (WTO) model

Should it prove impossible to negotiate a FTA, or other form of preferential trade agreement, then trade would revert to reliance upon WTO 'most favoured nation' (MFN) rules. Trade between the UK and EU would no longer be free from restriction, but rather be based upon tariffs no higher than those offered by the EU to other nations. Calculated on a trade-weighted basis, the EU's average tariff is only around 2.3% for non-agricultural goods[2], which is a relatively modest level and should prove to have only minimal cost implications for UK exporters. This average figure, however, obscures the fact that, for certain sectors, the tariff rates are significantly higher. Vehicle production, for example, may face tariffs of around 8.5%, whilst plastics are likely to face a tariff of 5.9% and beverages 8.5% (Business for Britain, 2015:777-8). It should be noted that, since the value of Sterling has depreciated by more than 12% since the European referendum result, none of these increases in tariff costs would offset the boost to international competitiveness resulting from this shift in the exchange rate. Moreover, independence from EU rules would enable the UK government to offset any negative impact, through a range of other measures taken to enhance the competitiveness and productive potential of the UK industrial base. These could include additional tax credits to stimulate R&D, or measures to enhance technical skills formation.

The WTO model provides the UK with the greatest policy flexibility but greater restrictions placed upon continued access to EU markets. Nevertheless, given the relatively modest level of average MFN trade-weighted tariffs that would be levied, the price for gaining this additional degree of policy autonomy might be considered to be worthwhile by UK policy makers. Indeed, this is probably the meaning of UK Prime Minister's comment that "no deal for Britain is better than a bad deal for Britain"[3].

4.3 Membership of NAFTA

There are compelling reasons why both the US and the UK should actively promote closer cooperation; potentially even culminating in the UK joining the North American Free Trade Agreement (NAFTA) comprising the United States of America, Canada and Mexico (United States International Trade Commission (2000); Baimbridge et al., 2004; Philippidis, 2004). NAFTA countries have already expressed interest in establishing closer trading relations with EFTA and Chile. If Britain participated in such a grouping, a revamped NAFTA could ultimately be transformed into a global free trade association, which could potentially incorporate such countries as Australia, New Zealand, South Africa, Denmark, Sweden, Norway, Ireland, Switzerland, together with the Caribbean. It would be a grouping, based solely upon a commitment to free trade between them. It would seek no control of member states' trade relation with non-members nor would it possess the motivation to pursue 'ever closer union' that renders the EU unpalatable to many people within the UK. By contrast, NAFTA would prove more consistent with the democratically accountable sovereignty of each individual participating nation state.

The UK and the US economies are closely intertwined through trade, investment and the business cycle; so that further trade liberalisation would result in immediate benefits, in terms of trade creation, for both. From the past, the US and UK share a common culture and language, which make a contemporary trade relationship between them more likely to prove successful. A free trade area centred on an Anglo-American nexus is a more efficient fit than any conceivable alternative economic arrangement.

One important factor for potential partners in a free trade area to consider relates to the degree of comparability of the economies in question. In particular, what possibilities for economies of scale exist for firms taking advantage of the larger free trade area, and whether trade creation will exceed trade diversion resulting from the creation of the larger trade bloc. The former benefit will result from companies currently stymied from expanding to their optimum size due to the limited size of the domestic market, and therefore are unable to offer consumers products as cheaply as would be the case in a larger market. This potential for lower prices will also be more likely to be realised in a larger market, where competition will prevent former national monopolies or oligopolies from exploiting their market power and maintaining high prices.

A second type of potential benefit accruing from the enlargement of NAFTA would refer to the degree of trade creation less diversion. This relates to the fact that, in a global market characterised by free trade, the most efficient producer(s) in a given commodity should specialise in its production, thereby optimising consumer benefits from low prices and efficient production. However, the existence of trade restrictions (i.e. tariffs) means that less efficient internal producers might be able to produce goods and services more cheaply, thereby transferring production from more to less efficient companies, and consequently wasting precious resources through this unwarranted diversion of trade. The benefit of a free trade area is where former tariffs levied on foreign firms now inside the tariff barriers might result in more efficient producers taking market share from less efficient domestic firms, thereby consuming less scarce resources and thus potentially increasing world production.

Since its withdrawal from the ERM, the British economy has been convergent, both structurally and cyclically, with North America. Consequently sterling tracks the US dollar not the euro, whilst its divergence from continental euro has widened. Thus sterling has fluctuated in a range of 13% against the dollar since September 1992, but over a range of 37% against the (former) deutschemark. Such oscillations determine the efficiency of interest rate harmonisation, leading to the conclusion that the American and British economies are more convergent with each other than either is with the euro zone. Such a conclusion is supported by analysis of the growth rates of the UK, the US, France and Germany.

In terms of business cycle, the UK has traditionally had a closer statistical relationship with USA than with Germany and other leading EU member states (Bayoumi and Eichengreen, 1993). Indeed, whilst the US and UK economies have enjoyed years of relatively rapid economic expansion, many continental EU economies have been trapped in conditions of slow economic growth and high unemployment. In the decade prior to the Global Financial Crisis / Great Depression, the US created 22 million new jobs, while UK unemployment stood at a twenty year low. Comparable unemployment figures for leading EU member states were 9.1% in Germany, 11.7% in France and 12% in Italy, while standing at approximately 5% for the UK and US.

Additionally, a noticeable change in both US and UK economies has been the transition in their respective labour markets. The shift towards non-standard contracts, whether part-time, temporary or fixed-term working, together with the deregulation of the labour market, has increased the flexible adaptation of both economies to deal more effectively with industrial restructuring. One notable feature of this change is a decline in the non-accelerating inflation rate of unemployment (NAIRU) that denotes that level of unemployment associated with a stable rate of inflation. Consequently, both economies have little tendency towards inflationary wage pressure despite low unemployment levels. Moreover, productivity has been rising quickly in both nations, with US productivity growth outstripping average wage growth. This, together with the high value of both currencies, has dampened remaining inflation pressure from increasing oil prices and property market booms.

One factor stimulating productivity increases, running at double the average of the previous 25 years in USA, is due to the impact of information technology. One estimate calculates that computers account for about a quarter of the overall increase in productivity, with increases in the use of information technology accounting for approximately half of this rise. The UK accounted for 44% of all EU venture investment in high technology, with Germany a poor second with 17% of the investment total. The diffusion of information technology and especially the internet throughout the economy is incomplete, thereby allowing for continued high rates of future economic expansion. Stock market asset expansion has further stimulated consumer expenditure, with high technology shares securing the greatest value accumulation, before more recent market adjustment.

Macroeconomic strategy is similar for the UK and US, with restrained fiscal policy enabling a greater role for monetary policy loosening to facilitate economic growth and increased levels of investment though lower real interest rates. Supply-side policy seeks to reduce taxation to encourage entrepreneurship, together with stimulation of investment in human capital. Consequently, both nations are ranked in the top ten most competitive nations in the world; the USA maintaining its premier position. Moreover, of the most competitive EU nations it is the smaller Scandinavian economies that tend to score well in the World Economic Forum international competitiveness index, with the larger continental EU member states such as France, Germany and Italy receiving significantly poorer rankings.

Furthermore, if Britain joins NAFTA, the larger group will help to protect both the US and the UK from whatever outcome emerges from the EU experiment in supranationalism where a more broadly-based NAFTA can counter the impact of either an imploding, or a successfully integrating but by necessity largely inward-looking, EU. Third, the telecommunications revolution has led to the 'death of distance'; sharing borders no longer necessarily translates into increased trade and financial transactions, compared to a geographically distant country, as it has tended to do throughout history. A US-UK focal trading relationship would not work well in the era of the sailing ship or even when the Treaty of Rome was signed in 1957. Today information technology makes it eminently practical.

It is, moreover, possible that a revamped NAFTA could ultimately be transformed into a global free trade association. It would seek no control of member states' trade relations with non-members nor would it possess the motivation to pursue 'ever closer union', but respect each member's democratically accountable sovereignty. The last point is important because the now stalled Trans-Atlantic Trade and Investment Partnership (TTIP) contains clauses that are problematic for the ability for future democratically elected governments to protect the integrity of the NHS, public services and indeed any publically owned industries, from penetration by large US trans-national corporations[4].

4.4 Commonwealth FTA

The greatest visible sign of economic weakness is the persistence of mass unemployment within EU nations, which is not matched by the North American, Asian 'Tiger' and Latin American areas. Indeed, it is interesting to note that many Commonwealth countries offer potentially faster growing markets than do other EU member states and hence the development of a Commonwealth free trade area. Indeed, Commonwealth nations include a number of the fastest growing markets in the world, particularly in South and East Asia (World Bank, 1993) where historic links may give the UK a potential advantage in re-establishing trade links with these dynamic economies (Burkitt and Baimbridge, 1990; West, 1995). Again the potential exists to develop the Commonwealth into a FTA, since for too long the UK has been distracted from taking advantage of such export opportunities by the emphasis focused upon trading with European neighbours and by the EU’s common external tariff, which encourages other nations to place tariffs upon EU exports, thereby putting UK companies at a competitive disadvantage with the rest of the world.

Historic links with Commonwealth nations could give the UK a potential advantage in establishing trading links with these dynamic economies. These include Singapore, India, Pakistan, Malaysia, New Zealand, Australia, Canada and the ‘new’ South Africa. This trade potential is likely to have become even more favourable as those regions with close Commonwealth connections outperform the IMF’s estimated world growth rate of 3.7%, whilst the USA, Eastern Europe and non-EU industrial countries were all anticipated to grow faster than the EU. Indeed, the World Bank (1993) estimated that the areas of the world which grew most during the past two decades, namely South and East Asia, will continue to expand more rapidly. Additionally, growth potential is expected to result in significantly higher rates amongst most developing, than amongst the developed, economies. Latin America, Africa and the Middle East join Asia in offering UK companies superior potential for increased export sales than does the EU single market. Brexit highlights these developments in the world economy and reduces the danger of the single market distracting UK firms from pursuing their widest options for sales and discourage a parochial European mentality at a time when a more international focus is indicated, for both short- and long-term trade prospects.

Naturally enough, predictions relating to future market shares must always be taken with more than a degree of scepticism due to the tendency to fail to predict external, or even internal shocks, which may alter national growth and competitiveness figures substantially. Suitable examples concern currency and financial crises involving EU member states in 1992, Asian economies in 1997 and Russia in 1998. Nevertheless, even including these effects, East Asia appears likely to expand more rapidly than continental EU economies over the next few years, and therefore trade relations are more likely to grow in importance over this medium-term time period.

5. Conclusion

Even in light of the 2017 General Election outcome where the incumbent Conservative Party failed to receive the mandate regarding Brexit that it was seeking in terms of a larger parliamentary majority, the arguments contained in this chapter remain valid concerning the potential alternative trade relationships that Britain could pursue, where each possesses advantages and disadvantages. Hence, the choices made by policy makers needs to be mindful of this potential trade-off between policy autonomy and trade access, and a final selection should rest at least partly on the basis of a cost-benefit analysis following an informed public debate.

Whichever option is selected, the crucial common factor is that it permits the UK sufficient freedom to craft an independent economic policy based upon national priorities and interests, thereby enabling the formation of new trade relationships that better represent the dynamic elements of the world economy.

Rather than being tied into regional economic integration, where distinctive areas of British competitive advantage are sacrificed in pursuit of harmonisation across the European continent, British workers and companies could benefit from a change in focus, from a narrow vision of the future, to a global, more enriching alternative.

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Notes

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