

Author's note and acknowledgements

Author's note

I have written 'Spotlight on Services' with a non-expert reader in mind – someone who would simply like to understand UK services trade better.

In discussions with friends, I often find they are unsure about what services trade covers, or how it is being affected by the UK's trade agreement with the EU. It's challenging for casual observers, because commentators and journalists tend to focus on goods instead of services and frequently quote different trade statistics.

On the third anniversary of the UK's trade agreement with the EU, it's a good time to take stock, particularly as the trade disruptions due to Covid have largely subsided.

Superficially, services exports look healthy, but below the surface there's more to see....

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January 2024 (September 2023 article updated)

Acknowledgements

Many thanks to Professor L. Alan Winters, John Hawksworth, David Corless and David Henig for reviewing earlier drafts and providing very helpful comments and suggestions. Thanks also to staff at the Office for National Statistics for answering my queries.

About the author



I am an independent management consultant and specialises in risk and regulation in financial services. I also write occasionally on wider Brexit issues and created [BrexitFactBase](#).

After a career as a finance director and in consulting with PwC, I advise Hogan Lovells clients as part of the financial services regulatory consulting team.

Spotlight on services

Introduction

Services trade statistics might look healthy at first glance, but there is no room for complacency. The UK often reassures itself that it is a ‘services superpower’, as the second global services exporter after the US, but other countries are catching up fast.

Services are crucial for the UK economy - they account for over half of UK exports and a growing share of total trade. Exports are critical for well-paid employment, supporting around 6.5 million jobs, which are generally more productive and better paid than equivalent jobs¹.

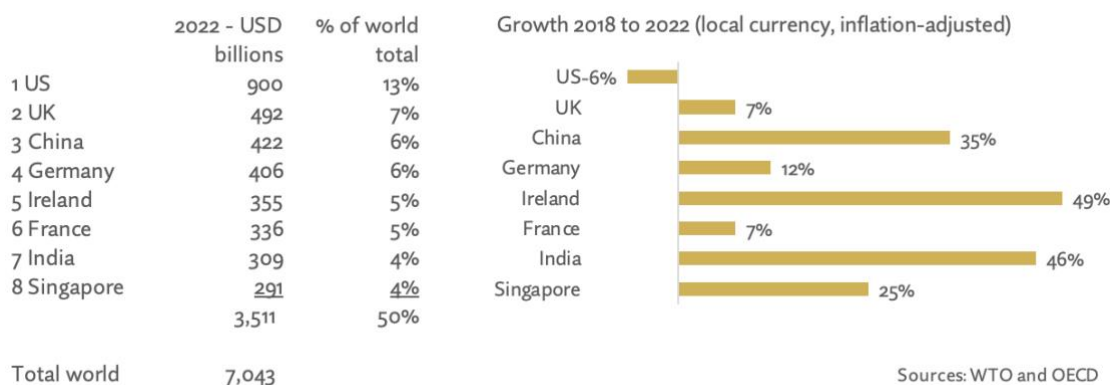
As the trade disruptions due to Covid have largely subsided, the data is starting to reveal the consequences of leaving the EU - the UK’s most important market.

This short report assesses the impact by comparing exports to the EU with those to other destinations². Delving into the data shows that the Trade and Cooperation Agreement (TCA) is harming exports to the EU for most, but not all, service types. However, the damage seems to be going unnoticed, probably because it is hidden by inflation and better performing exports to non-EU countries.

Global position under threat

In 2022, the UK was second only to the US in service exports (Figure 1)³. This is an enviable position because global services trade, driven by digital services, is growing faster than goods trade. However, the UK’s position is under threat. China is close behind, followed by Germany, Ireland, France, India and Singapore.

Figure 1 – Leading global exporters of services in 2022



¹ [Estimating the relationship between exports and the labour market in the UK](#), Department of International Trade, March 2021. Figure relates to 2016 for goods and services exports.

² [International trade in UK nations, regions and cities: 2021, June 2023](#). ONS recommends 2018 as the base year because it was the last year of stable trade patterns before Brexit effects.

³ [World Trade Organisation \(WTO\)](#) trade statistics for commercial services (accessed January 2024)

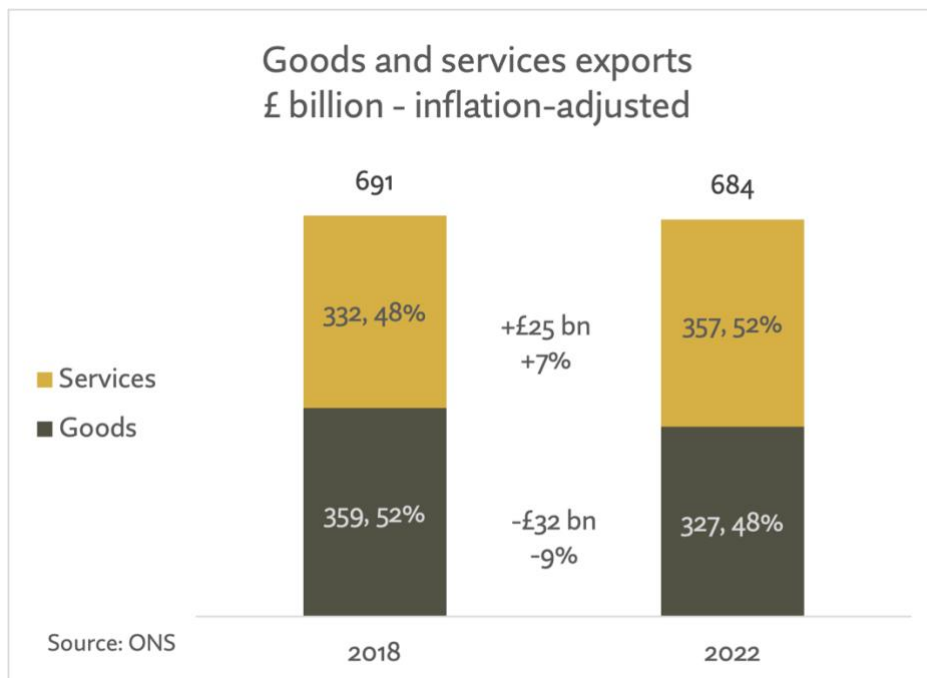
Since 2018, the UK grew services exports by 7%⁴. Other leading services exporters had much higher growth rates (notably China at 35%, India at 46% and Ireland at 49%) and, as the WTO found, are growing much faster than the UK in digitally delivered services - the main driver of future growth⁵.

UK trends

UK services exports look healthy overall, rising by £25 billion (7%) between 2018 and 2022 in real terms (Figure 2) - economists prefer to use inflation-adjusted or ‘real’ prices.

In 2018, services accounted for 48% of all UK exports, and, by 2022, that share had grown to 52%, partly because goods exports had fallen by 9% (£32 billion)⁶.

Figure 2 – UK goods and services exports



Politicians prefer to quote current price statistics because inflation flatters results. Last February, Business and Trade Secretary, Kemi Badenoch, welcomed figures showing UK services exports had reached record highs, adding that they ‘cement the UK’s position as a global services superpower’⁷.

⁴ Organisation for Economic Co-operation and Development (OECD) Quarterly National Accounts plus India and Singapore government statistics (accessed January 2024)

⁵ [World Trade Organisation Trade Outlook](#), April 2023, 2022 vs 2019

⁶ See note 8 for ONS data. The ONS statistics for UK-EU goods trade reflect measurement methodology changes in 2021. This creates a discontinuity in 2021 but after careful consideration the ONS recommends no adjustment to pre-2021 figures. (see [Impact of trade in goods data collection changes on UK trade statistics: summary of adjustments and the structural break from 2021](#)).

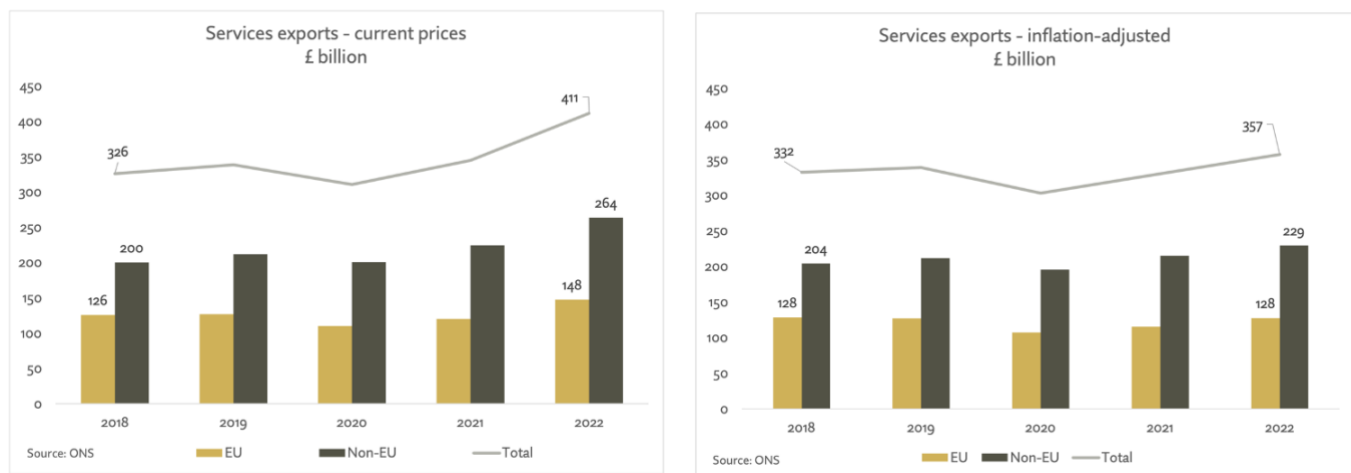
⁷ [Department of International Trade](#)

Indeed, measured in current prices, the trend in total services exports looked particularly strong (Figure 3⁸- left-hand panel). Despite the Covid dip in 2020, UK services exports grew by 26% (£85 billion) from £326 billion in 2018 to £411 billion in 2022⁹.

Adjusted for inflation, the overall trend still seems healthy with growth of 8% (£25 billion) from £332 billion to £357 billion (right-hand panel). However, the growth came from non-EU exports while UK exports to the EU stayed flat at £128 billion.

In the same period, the EU grew its *imports* of services by 18% in real terms.¹⁰ This means UK services exports to the EU have dramatically underperformed. In the absence of other factors, it seems likely that Brexit has had a major effect. Before jumping to conclusions, let's look at the data in more detail.

Figure 3 – UK services export trends 2018-2022



Main service types

To understand the performance of UK exports to the EU relative to the rest of the world, we need to delve into the main service types¹¹. To make our analysis manageable we focus on the top six which accounted for 72% of total services exports in 2018. These six service types were financial, professional, personal travel, affiliates and intragroup, transportation, and telecoms, computer and information services (for the full picture, see Figure 5 at the end of the piece).

Effects of the TCA on goods

Goods and services trade are frequently linked, so it's important to recognise the effects of the TCA on goods exports and the consequences for services.

⁸ [ONS](#), UK trade: goods and services publication tables, published December 2023.

⁹ [ONS](#), UK trade in services: service type by partner country, non-seasonally adjusted, October 2023.

¹⁰ [OECD](#), Quarterly National Accounts, chained volume measures. EU import growth includes intra-EU (accessed January 2024).

¹¹ ONS uses standard international categories for services trade. Figure 6 details the ONS categories.

A third of UK goods exporters directly export services, often by packaging them together. A well-known example is [Rolls Royce](#) where services are more than half of sales. Since the introduction of the TCA, UK goods exports have been down across the board compared to other G7 countries¹². While other G7 countries have experienced a relative boom in goods trade, UK goods exports to the EU in 2022 were down 9% (£15 billion) on 2018, inevitably harming the direct services sold alongside, such as finance and distribution, and lowering future services sales.

There is also a subtler relationship between goods and services exports that usually goes unremarked. [Over 20% of the value of UK manufacturing](#) exports comes from embedded services, for example the engineering and software services in a car. However, the value of embedded services is included in the value of goods exports – it does not appear as services exports. This means a drop in manufacturing exports reduces services exports by more than any fall shown in the services trade statistics.

New trade barriers for services

Services trade was the poor relation in the Brexit negotiations. Although the TCA has welcome provisions for digital services, intellectual property and a chapter on legal services, it ignores key areas for UK exports such as financial and professional services beyond basic WTO terms. This is probably because the political focus of the Brexit negotiations was on eliminating tariffs from goods trade. As a result, and in the face of resistance from the EU, services were largely ignored.

The TCA erects a range of barriers for services exports, which include:

- restricted mobility of people (through limited duration of visits, work permits and visas etc.);
- lack of mutual recognition of professional qualifications;
- loss of passporting rights (notably for financial services firms); and
- loss of road and air transportation rights.

We can highlight those barriers which are most important for individual service types and take a view on the likely consequences¹³.

Results by service type

Figure 4¹⁴ shows the makeup by service type of the 12% (£25 billion) rise in non-EU exports and zero growth in UK exports to the EU.

Two broad messages stand out – lower growth in EU exports where non-EU exports grew and, where non-EU exports shrank, greater shrinkages for EU exports.

¹² Other G7 goods export growth rates for 2022 over 2018 were Canada -4%, France -3%, Germany +4% Italy +11%, Japan +6%, US +3% (OECD). UK goods exports to EU and non-EU countries were both down by 9%.

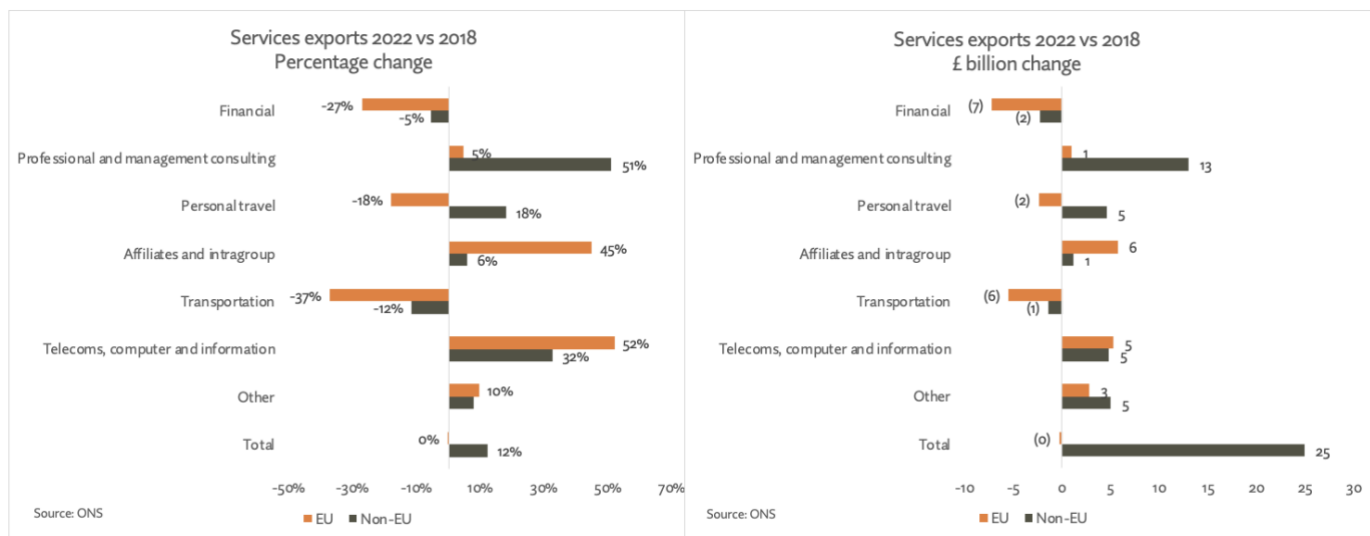
¹³ A more detailed study could isolate and quantify Brexit effects more precisely.

¹⁴ ONS provides an EU/non-EU split in CVM terms by major category of service type in its [Breakdown of Trade](#) (December 2023). Where required, the EU/non-EU split for sub-categories is derived from the more detailed services exports figures available in [current prices](#).

The two biggest UK services exports to the EU, financial services and professional services, markedly underperform non-EU exports. Similarly, personal travel and transportation exports to the EU are missing out.

By contrast, exports to the EU outperformed for telecoms, computer and information services, as did exports to EU affiliates (companies in the same group).

Figure 4 – Changes in UK services exports between 2018 and 2022



1 Financial services saw a 27% (£7 billion) fall in exports to the EU and a smaller non-EU fall of 5% (£2 billion). Loss of passporting means that UK-regulated services firms can no longer export freely to the EU. In response, several international banks now use EU-regulated firms based in, say, Paris, Dublin or Frankfurt instead of London, to serve EU customers. As the delighted governor of the French central bank [said](#) in July, ‘Paris’s post-Brexit success has been spectacular’.

2 Professional services EU exports grew by 5% (£1 billion) in contrast to the 51% (£13 billion) increase in non-EU exports, mainly in the US (see Figure 4). UK exporters now face a patchwork of member state rules on qualifications and visa requirements, which makes exporting complicated and encourages EU customers to choose EU-based suppliers. The results are stunted growth in professional services exports to the EU and a shot in the arm for EU competitors. Simultaneously, some UK exporters seem to have pivoted from the EU to the US.

3 Personal travel EU exports fell by 18% (£2 billion) as non-EU rose by 18% (£5 billion). Travel exports represent expenditure in the UK from foreign visitors and students coming to the UK. However, TCA mobility restrictions make it harder for EU citizens to visit or study in the UK. In addition, a big jump in university fees for EU students, starting in the 2021/22 academic year, made the UK less appealing.

Behind the headline numbers, there was a 37% (£1 billion) fall in education-related travel from the EU and a 14% (£1 billion) fall in other personal travel. Non-EU exports in

education travel grew by 23% (£3 billion) and exports in other personal travel grew by 13% (£2 billion). The new visa restrictions announced in January are likely to impact all education-related travel exports.

4 Exports to EU-based affiliates (related companies in the same company group) rose by a dramatic 45% (£6 billion) whereas non-EU exports rose slightly by 6% (£1 billion) (see Figure 4). Some of the rise is related to the falls in other service types, as UK exporters restructure their operations to cope with being a ‘third country’ outside the EU. Rather than export directly to EU customers, some now supply services to an EU-regulated entity. For example, easyJet’s new [Austrian subsidiary](#) operates flights between EU member states but buys its seat capacity from [easyJet UK](#).

5 Transportation exports to the EU fell by 37% (£6 billion) whereas non-EU exports fell by 12% (£6 billion). Fewer goods exports to the EU were a factor. In addition, British airlines and road hauliers now have no right to provide services within the EU, and limited rights for drop-offs and collections on trips from the UK.

6 Telecoms, computer, and information services brought good news as exports to the EU rose by 52% (£5 billion), exceeding the non-EU rise of 32% (£5 billion) (see Figure 4). The TCA’s digital-trade provisions support exports to the EU, particularly as [digital services](#) are increasingly important. Negotiation of similar provisions would have helped other service types. Even on digital services, the UK remains hostage to the EU renewing its temporary grant of data adequacy in 2025. Failure to renew would introduce hefty [compliance costs](#) and decrease competitiveness.

Digitally delivered services can still be hampered by other trade barriers to the single market. For example, a UK digital challenger bank cannot simply provide digital services to EU customers. It must now have a physical presence in the EU, which involves additional investment, extra operating costs, and an extensive authorisation process with an EU banking regulator.

Major change required

This high-level analysis shows that the TCA is constricting exports to the EU. A more detailed study could quantify the effects more precisely, but it’s clear there’s a major issue.

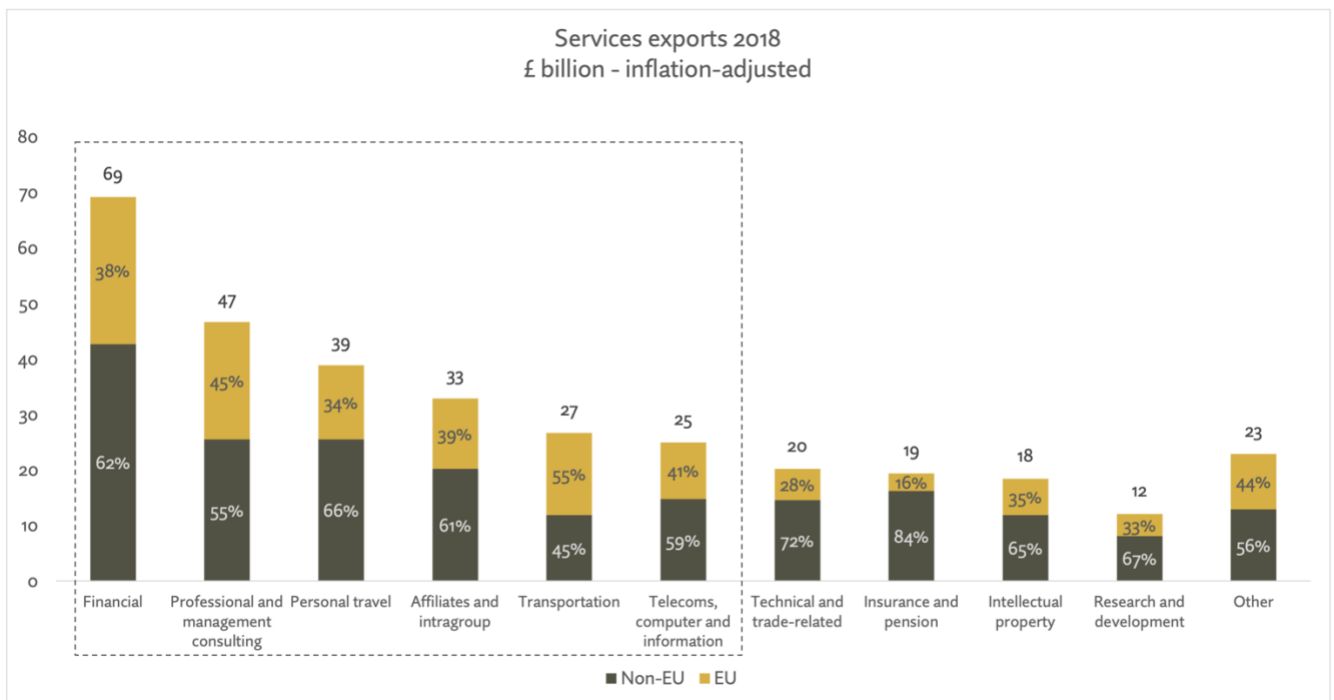
Loosening Brexit’s grip on both goods and services would significantly boost services exports to the EU. Freer trade with the EU would also reinforce the UK’s global services position, which seems destined to deteriorate as the TCA’s harms accumulate.

Refinements to the TCA, such as the Labour Party’s proposals, will help, but they involve cautious tinkering rather than an ambitious step change to bring the UK much closer to the EU single market - the UK’s largest trading partner.

Leading politicians should acknowledge the serious consequences of the TCA for services trade and that change is needed. Without major reform, UK services exports to the EU will continue to underperform, the UK’s competitive position will continue to weaken, and economic growth will be harder to achieve.

Supporting data

Figure 5 – UK services export profile in 2018 with EU and Non-EU split



In 2018, total services exports were £332 billion with the top six service types shown here producing £239 billion (72%).

Note that the non-EU share of exports was greater than the EU share for all service types, apart from transportation. This helps protect the UK against reductions in its EU exports and provides growth opportunities.

The ONS category ‘Other Business Services’ (OBS) accounted for £112 billion (34%). Figure 5 shows the four main sub-categories of OBS: professional and management consulting (£47 billion), affiliates and intragroup (£33 billion), technical and trade related (£20 billion) and research and development (£12 billion).

Figure 6 – Allocation of ONS categories to service types¹⁵

7: Financial	
	7.1: Explicitly charged and other financial services
	7.2: Financial intermediation services indirectly measured (FISIM)
10.2: Professional and management consulting services	
	10.2.1.1: Legal services
	10.2.1.2: Accounting, Auditing, Book-Keeping and Tax Consulting
	10.2.1.3: Business and management consulting and public relations services
	10.2.2: Advertising, market research and public opinion polling

¹⁵ Reference numbers relate to ONS categories for trade statistics. Other Business Services is 10.

4.2: Personal travel	
	4.2.1: Health-related personal travel
	4.2.2: Education-related personal travel
	4.2.3: Other personal travel
10.3.N: Affiliates and intragroup	
	10.3.N59: Services between affiliated enterprises not included elsewhere (n.i.e)
	10.3.N510: Intragroup fees and cost recharge
3: Transportation	
	3.1: Sea transportation
	3.2: Air transportation
	3.3: Other modes of transportation
	3.4: Postal and courier services
9: Telecommunications, computer and information services	
	9.1: Telecommunications services
	9.2: Computer services
	9.3: Information services
10.3: Technical, trade-related and other business services	
	10.3.1: Architectural, engineering, scientific and other technical services
	10.3.2: Operating leasing services
	10.3.3: Operating leasing services
	10.3.4: Trade-related services
	10.3.5: Other business services n.i.e.– excluding affiliates and intragroup
6: Insurance and Pension	
8: Intellectual property	
10.1: Research and development services	
Other	
	1: Manufacturing
	2: Maintenance and Repair
	4.1: Business travel
	5: Construction
	11: Personal, Cultural and Recreational
	12: Government

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