Resolution Foundation

Trading blows

How should Britain buy and sell in a turbulent world?

Emily Fry & Sophie Hale

December 2024

Acknowledgements

With thanks to Abi Millis for research undertaken on the trends in goods and services trade as part of a short secondment to the Resolution Foundation. Contributions to this report from colleagues at the Resolution Foundation are gratefully acknowledged, particularly those from Mike Brewer, Tom Clark, Rob Holdsworth, Greg Thwaites, and Simon Pittaway. Thanks also to Ingo Borchet, Martina Magli, as well as colleagues at the Department for Business and Trade for their feedback on the analysis that informed this report. All views and any errors remain those of the authors

Download

This document is available to download as a free PDF at: resolutionfoundation.org/publications

Citation

If you are using this document in your own writing, our preferred citation is: E. Fry & S. Hale, *Trading blows: How should Britain buy and sell in a turbulent world?* , Resolution Foundation, December 2024

Executive Summary

These are anxious times in global trade, and the UK has particular reason to worry. Before the dust has settled on one great disruption – Brexit – Donald Trump, with talk of sweeping tariffs, threatens another. This report asks what our economic experience of the first might teach us about how to handle the second.

Brexit so far has turned out to be a tale of two sectors: while traded services have held up surprisingly well, Britain's goods trade has proved vulnerable. The incoming American administration's protectionism aims squarely at goods, threatening a second hammer blow there. The 10-20 per cent generalised tariffs that Trump has floated are of equivalent scale for goods exports to the US to the non-tariff barriers that Brexit imposed on goods sales to the EU. The knock-on effects could be darker still if Trump's mooted super-tariffs on rivals such as China combine with retaliation to lurch towards global trade tension or even, in the extreme case, a truly global trade war. No longer part of a large trading bloc, the UK would then face sharp dilemmas in a scramble to retain access to overseas markets and its flow of imports.

Bad times for goods

It's a very long time since Britain was 'workshop to the world', but the recent relative slide in its goods trade has been intense, with the value of UK goods exports rising by just 0.3 per cent each year since 2019, far below goods export growth across the OECD of 4.2 per cent annually over the same period. Indeed, the only sector larger in 2023 than 2007 in export volume terms is machinery and transport. Brexit effects are evident in various ways, including falling EU sales from smaller traders, on whom the fixed costs of new paperwork weigh heavily.

And there's no room for complacency about the further disruption, which the Trump tariffs (and reaction to them) threaten. Even in its relatively shrunken form, manufacturing remains a crucial source of 'good jobs', with pay at middling or better rates. Exports account for around a quarter of final demand, far more than for services. The Government's Industrial Strategy recognises the particular role of 'advanced' manufacturing, and yet the UK's exports are increasing slowly in what should be growth fields, such as motor vehicles, as well as in areas of UK comparative advantage, such as pharmaceuticals. Disrupted imports are just as much of a threat for UK industry – which is embedded in international supply chains – and to all of us as consumers. All told, 60 per cent of all the goods we use – whether as inputs into domestic industry or consumed by government or households – are foreign-made. That means any UK recourse to tariffs within a trade war would be costly.

Indispensable invisibles

In the distant past, trade in services was something of an afterthought – they were described as 'invisibles' on the balance of payments. Today, overseas service sales are central to Britain's prospects. Services as a whole account for more than 80 per cent of UK output, giving them a dominant bearing on family finances. And although services as a whole remain less exposed to trade than goods, Britain's mighty finance sector is actually today more export-intensive than manufacturing. Services overall provides the majority – some 54 per cent – of UK exports. All this makes the UK a 'service superpower', selling more internationally than any other country except the US.

Brexit looked like it could be a big problem. The services trade barriers implemented post-Brexit are high in some areas, because the Free Trade Agreement between Britain and the EU is, like most such agreements, overwhelmingly focused on goods. But, despite this, by increasing sales beyond Europe and nurturing sectoral strengths, the UK has maintained a buoyant overall export performance: its total share of OECD service exports has risen by 0.9 percentage points since 2019.

The UK needs to keep this up. For a medium-sized economy, sales into a growing global service trade have huge potential to grow. While a large chunk of direct rewards accrue at the top of the income scale, some major exporting areas, such as education, employ substantial numbers of poorer and middling families. Much more generally, service exports buoying incomes across a local economy translates into local demand and thus more and better earning opportunities in non-tradable services (think of local restaurants or beauticians).

The UK's service exports now break pretty evenly between the EU (£170 billion), the US (£126 billion) and the wider world (£172 billion). The recent growth has been powered along by strong American sales, and rocketing service exports to India, which are up three-fold since 2016 (+215 per cent).

Long-established UK strengths (such as insurance and 'other business services') have been important in recent growth. Also important are two specific 'workarounds' to traditional barriers to trading services. One is remote trading, without people moving. Very often this involves digital channels, which were given a tremendous boost of necessity during the pandemic. Right across Britain's big service industries, more overseas trading is now done this way than by workers heading abroad or customers (such as tourists) heading to the UK. The 'remote' proportion of direct services exports (i.e. non-subsidiary sales) rose from two-thirds (65 per cent) to about three-quarters (72 per cent) since 2019. For the giant 'other business services' category, the share has risen from 70 per cent to 81 per cent, extending an established trend of digital trade sharply reducing services trade costs.

An even more significant workaround involves companies setting up subsidiaries to trade in foreign markets: two thirds (66 per cent) of all UK services sold abroad were supplied this way in 2019. Some sectors hugely ramped up this approach after Brexit: in Information and Communication, for example, the share of total trading (exporting and importing combined) done through affiliates increased by 4.1 percentage points post-referendum compared with pre-referendum, even controlling for trends over time and sector. Others – such as Professional, Scientific and Technical fields – either couldn't or didn't adapt in the same way.

Both types of workarounds have facilitated export growth. Those fields, like 'other business services,' that have strongly pivoted to digital have thrived (with the volume of total exports up from £65 billion in 2007 to £153 billion in 2023) while others which were less able to do so have stagnated. Consider Transport, which is linked to the physical presence of people and equipment, and also strongly intertwined the goods trade: its exports fell from £25 billion to £21 billion over the same years.

Reasons to be fearful

Britain's service trade has come through Brexit surprisingly unscathed overall, and it is not directly targeted by Trump's potential tariffs. And yet it cannot be assumed that recent growth will continue. For one thing, there are tentative signs – in some sectors at least – of customers getting 'Zoomed out' by all the digital trade. Both service exports as a whole, and those booming 'other business services' in particular, saw the share of digital sales slip back somewhat between its pandemic peak and 2022, with declines of 10 and 8 percentage points respectively. Another concern are regulatory barriers, which are already impeding export potential in some areas: the overall growth in service exports has come disproportionately from unregulated fields. Advertising and market research is one example: its exports more than doubled (up by 128 per cent) between 2015 and 2022. In total contrast, some big sectors which require workers to have professional qualifications in every jurisdiction they operate in have seen exports grow slower than the average services sector: consider accounting, for example, whose foreign sales grew at a comparably modest 39 per cent over the same years, or legal services which has seen growth of 35 per cent.

All this is before we consider the potential consequences of a world mired in new conflicts over commerce. Geopolitical tensions or disputes over the tax treatment of subsidiaries or digital sales could spur states to put restrictions on both our 'workarounds' against trade barriers. Moreover, some services, such as software and after-sales support for advanced manufacturing are often intertwined with goods trade. They wouldn't escape a global goods trade war without serious damage.

Trading off

As ministerial minds turn towards a new trade strategy, due next year, they confront multiple and formidably difficult balancing acts. For a start, they will need to carefully apportion diplomatic effort between goods (where vulnerabilities warrant a broadly 'defensive' approach) and services (where a more 'expansive' strategy is warranted). Getting the right ratio of effort here is a delicate calculation even before we consider its potential to get caught on the horns of the looming geopolitical dilemma that Britain is desperate to avoid – the unwanted choice between trading with the US or with the EU.

If goods were the only issue, the over-riding strategy would be relatively clear: stay as open as possible as is consistent with holding your biggest trading partner close. That partner is still, overwhelmingly, the EU, from which we buy over half all our goods imports (£318 billion) and sell only a little less than half of our goods exports (£186 billion). The UK would obviously need to be pragmatic and grab any sector-specific deals the US and others may offer, so long as they could be had without jeopardising that crucial cross-Channel relationship. But from a goods perspective, it makes sense to hold fast to EU standards, even if this could complicate or even reduce the (already low) chances of an attractive general US-UK Free Trade Agreement.

The same logic could condition Britain's response to the Trump tariffs in goods trade. For the UK in isolation, the least-bad option might be living with tariffs, while being measured and selective about any retaliation, so that Britain's businesses and consumers continue to benefit from £58 billion of annual imports from the US. In a world of rising trade tension, however, such unilateral openness could be hard to sustain if the EU became anxious about the UK being a backdoor for goods from the US and beyond. The UK has already taken a very different stance towards China's electric vehicles than either the US or the EU, by continuing to allow them in with its (relatively modest) existing 10 per cent tariff. For a medium-sized country dependent on a nearby giant market for trading goods, there may be limits to the scope for such independence.

So there are potential conundrums even before we get to services, where UK interests are much more expansive and varied. Our analysis points to a host of important objectives. One is keeping those crucial 'workarounds,' subsidiaries and digital sales, running smoothly by proactively seeking new agreements to remove (and avoid creating) barriers to trade through these channels. A serious effort also needs to be made to allow regulated services finally to share in Britain's service export boom. Brokering mutual recognition agreements on professional qualifications is urgent, and something that the private sector cannot sort out alone. Hammering such deals out with giant European and American markets are both obvious priorities, but so too must be large growing markets, notably India and Singapore.

Fortunately, some of the testing features of goods trade – hard borders, physical checks, fears about ‘backdoor’ access – don’t arise in quite the same way for services. Nor is the service trade caught in the same political glare that Trump is shining on the merchandise trade. And thus in services there is less reason to fear Britain being forced to ‘choose’ between America and Europe. It can – and must – look freely around the world with an opportunistic eye for any takers for negotiating service deals, and be pragmatic too about the many different ways in which progress can be forged. The detail will be varied, often technical and rarely glamorous. It may not make headlines, but it will sustain the trade in services, which is, in the end, Britain’s brightest hope for the future.

Just as the dust is settling on the Brexit trade shock, Trump threatens another

It has been a turbulent few years for Britain's trade. In the midst of Covid, which caused disruptions to both in-person services trade (such as tourism) and goods trade (through supply-chain bottlenecks), Britain implemented its new trading relationship with the EU.

Now, even though the impacts of these trade disruptions continue to emerge, Trump is threatening another one with across-the-board tariffs on US imports. At the time of writing, there is talk of tariffs as high as 10-20 per cent on all US imports – with even steeper rates for goods from China, Mexico and Canada[1] – levels that far exceed those imposed during his first term.[2] For the UK, proposed tariffs would rival the scale of goods-oriented non-tariff barriers introduced under the Trade and Cooperation Agreement (TCA) going to and from the EU, though the US proposals would be confined to US-bound goods.[3]

Some want to catastrophise about what Trump tariffs might mean for Britain, but, as the Government turns its attention to developing its trade strategy, due next year, the key will be taking stock of Britain's trade, including how it has responded to disruptions in the past few years, and using that to understand how we might be able to navigate the future. This briefing note contributes to that by analysing the path of UK trade in the early 2020s, drawing lessons from recent shocks to suggest how the UK might fare through the rest of the decade.

As we set out in the rest of this note, the big picture is that trade in the 2020s has been a tale of two sectors: goods are struggling, services are holding up.[4] In the years following the implementation of the TCA with the EU in January 2021, the UK's goods trade has underperformed the OECD. UK goods exports haven't been performing particularly well for years, but their value grew by just 0.3 per cent each year since 2019, while the OECD's goods exports grew by 4.2 per cent annually over the same period. Meanwhile Britain's goods imports had been keeping up with the OECD prior to 2019. but have since grown at half the rate of the OECD at just 2 per cent each year, compared with 4.3 per cent for the OECD (Figure 1).[5]

1 Possible tariffs floated have ranged from 60 per cent on imports to the US from China and Mexico, to a 25 per cent tariff on all imports from Mexico and Canada, with 10 per cent extra for China. For more discussion, see: A Williams, Donald Trump says he will hit China, Canada and Mexico with new tariffs, The Financial Times, November 2024.

2 Back then, tariffs averaged around 20 per cent on just three-fifths of China's exports to the US, while imports from the rest of the world faced an average of just 3 per cent. C Bown, US-China Trade War Tariffs: An Up-to-Date Chart, The Peterson Institute, April 2023.

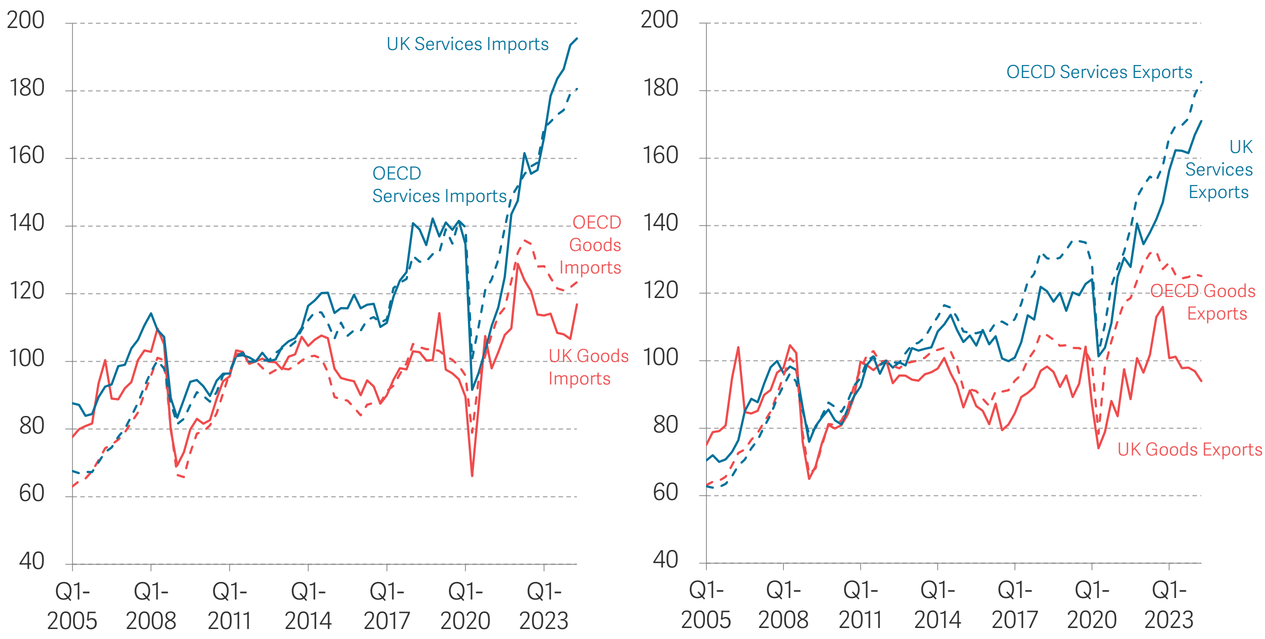
3 S Dhingra et al., Big Brexit: An assessment of the scale of change to come from Brexit, Resolution Foundation, June 2022.

4 In this note, we use sectors to refer to goods and services, as well as SIC breakdowns of these.

5 RF analysis of OECD, Balance of Payments, Revenue and Expenditure. Period compares 2019 with the full year of Q3 2023 to Q2 2024. Figures are in current prices and are USD exchange rate converted. In chained volume measures, excluding precious metals, the UK's goods exports shrunk by 3.4 per cent per year and goods imports by 1.4 per cent per year over the same period. RF analysis of ONS, Trade Time Series, November 2024.

FIGURE 1: **Despite Brexit, UK services trade has kept pace with the OECD**

Index of goods and services imports (left chart) and exports (right chart), current prices (2012Q1=100): OECD & UK



Notes: Current prices, seasonally adjusted. USD exchange rate converted. Data includes precious metals
Source: RF analysis of OECD, Balance of Payments, Revenue and Expenditure.

However, services trade overall has kept pace with the OECD post-Brexit. Since 2019, services imports have grown faster than OECD imports (7.1 per cent vs 5.8 per cent per year), and services exports have grown faster than OECD exports (7.5 per cent per year vs 6.1 per cent per year). This 'normal' performance in Britain's services is a surprise given the scale of services barriers implemented within the TCA. Indeed, trade barriers amounted to an increase in barriers of 21 per cent to services trade with the EU, and 13 per cent for goods trade. A range of modelling estimates (including from the Resolution Foundation and LSE's Centre for Economic Performance) suggested that trade in services sectors would be worse hit by Brexit than goods sectors.[6] So, matching the OECD's performance in services trade – and even outperforming it since 2019 – is far better than was expected.[7]

This briefing note analyses the path of UK trade in the early 2020s, drawing lessons from recent shocks as the Government turns its attention to developing its trade strategy, due next year.

6 S Dhingra et al., Big Brexit: An assessment of the scale of change to come from Brexit, Resolution Foundation, June 2022.
7 Outperformance was not simply because of the UK's industry mix in services. E Fry, S Pittaway & G Thwaites, Life in the slow lane: Assessing the UK's economic and trade performance since 2010, Resolution Foundation, June 2024.

Goods trade has been vulnerable

It has been a long time since Britain was the 'workshop of the world,' but the recent slide in manufacturing trade post-2019 has been severe. Indeed, more than half (12 of 22) manufacturing divisions had lower real terms 'domestic output at basic prices' in 2022 than in 2015, and just under half (10 of 22) of these divisions were selling less overseas.[8] Taking a longer view, the only goods sector larger in export volume terms in 2023 compared with 2007 is machinery and transport.[9]

Although the EU is the only place with which barriers went up in 2021, the weakness in goods trade has been broad-based. As shown in Figure 2, with the exception of Hong Kong, the UK's goods sales to the world have underperformed the growth in our major trade partners' goods they buy from the rest of the world since 2016. This includes weakness with EU trade partners like Italy and Spain, goods exports to which fell by 2 per cent and 3 per cent each year, as both countries increased their imports from the world by 6 per cent annually. But the UK's weakness in goods exports also extends to non-EU countries including the US, China and Gulf states like the UAE and Saudi Arabia. For example, the UK's exports to China didn't grow, at the same time as China's imports from the world grew at 6 per cent each year.

However, this does not mean that Brexit plays no role in the UK's goods underperformance. Decompositions show that the UK's underperformance isn't just because of lower demand for the industries we sell to the world.[10] Studies have estimated that the UK's goods trade is around 30 per cent lower with the EU since the UK left the EU's customs union and single market.[11] Difference-in-difference models have found a large drop in particular sectors trade with the EU, such as 'agrifood' and 'textiles and clothing'.[12] And the Brexit effects on smaller businesses look stark: EU sales by smaller traders – on whom the fixed costs of new paperwork weigh heavily – have fallen by 30 per cent, with up to 20,000 small businesses estimated to have stopped exporting altogether.[13] This weakens Britain's growth prospects, because these firms now face barriers that stifle their potential to grow into the nation's future scale up businesses.

8 RF analysis of Supply and Use tables, deflated using Domestic Output PPIs. In ONS SIC, industry sections which are broken down into 88 divisions (denoted by two digits) which are then further broken down into groups (denoted by three digits).

9 Different sectors have performed differently since 2015. Textiles, wearing apparel and leather products have shrunk by 4 per cent in exports and 7 per cent in output since 2015. But not all manufacturing has been struggling to export. Beverages manufacturing has grown 34 per cent in exports and 23 per cent in output since 2015. RF analysis of ONS, Supply and use tables, various.

10 E Fry, S Pittaway & G Thwaites, Life in the slow lane: Assessing the UK's economic and trade performance since 2010, Resolution Foundation, June 2024.

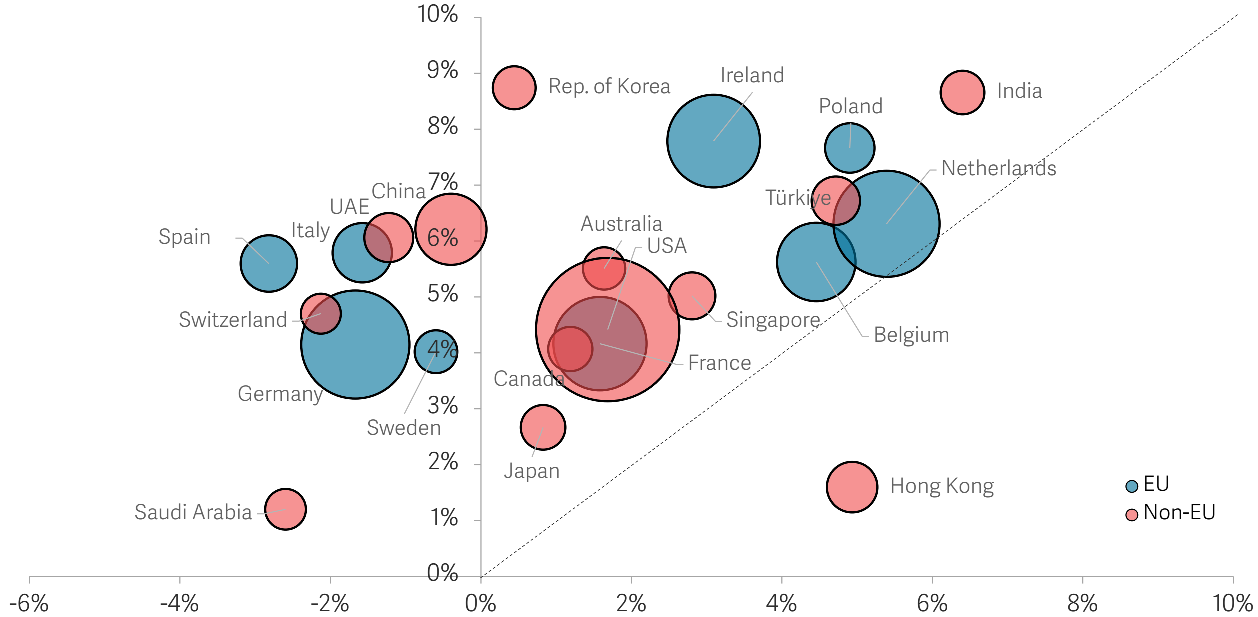
11 For example, evidence of the impacts of Brexit on goods trade using synthetic difference in difference and doppelganger models can be seen in: J Du et al., Unbound: UK Trade post-Brexit, Centre for Business Prosperity, Aston University, September 2024; J Springford The cost of Brexit: December 2021, CER, March 2022; J Portes, S Hall & S Hunsaker, UK trade 2024, UK in a Changing Europe, June 2024.

12 M Gasiorek ***& N Tamberi,*** Some goods (and some less good) news from UK trade, UKTPO, February 2024.

13 D Novy, T Sampson & C Thomas, Brexit and UK trade, June 2024.

FIGURE 2: **Goods export growth has been sluggish**

Annualised growth rate of UK goods exports and partner goods imports from world: UK, World, 2016-2023



NOTES: Current prices. Data excludes precious metals. Countries chosen in the top decile of UK goods exports by partner in 2023.
SOURCE: RF analysis of UN COMTRADE; ONS, Trade in goods: all countries, seasonally adjusted, November 2024.

Although manufacturing is a smaller part of the UK's economy than it used to be (8 per cent of jobs in 2024 compared with 15 per cent in 2000), this recent weakness in exports is worth worrying about, not least because manufacturing continues to be a source of 'good jobs' across the UK.[14] Workers in tradable goods industries are roughly 20 per cent more likely than average to have jobs in the upper-middle part – i.e. 50th to 90th centiles – of the wage distribution.[15] Compared to tradable services workers, tradable goods workers are also spread across the UK – for example, motor vehicle manufacturing is concentrated in Herefordshire, Worcestershire and Warwickshire, the West Midlands, and Northumberland and Tyne and Wear.[16] And exports are a more important source of final demand for goods overall than for services: about a quarter (23.3 per cent) of goods are exported, compared with 10.8 per cent of services.[17]

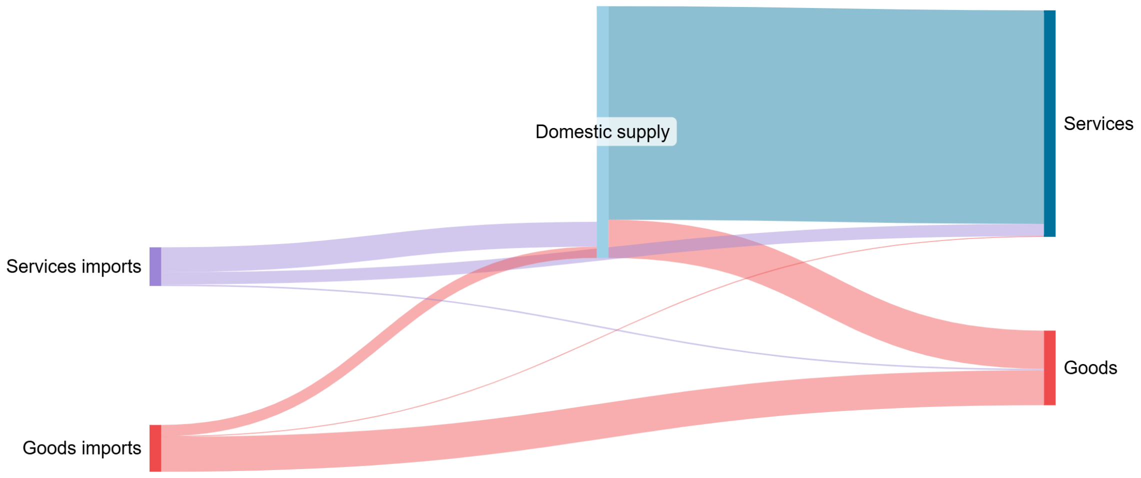
Worryingly, some of our advanced, high-productivity manufacturing is sinking in some sectors you'd think would be growth areas. For example, following the pandemic, many countries saw a boom in pharmaceuticals exports. With a large base of pharmaceuticals (14 per cent of the UK's manufacturing), and a historically sturdy revealed comparative advantage – a measure of the extent to which a country is specialised in exporting a specific product – you

14 RF Analysis of ONS, EMP13: Employment by industry, November 2024.
15 J De Lyon et al., Enduring strengths: Analysing the UK's current and potential economic strengths, and what they mean for its economic strategy, at the start of the decisive decade , Resolution Foundation, 2022.
16 ONS, The spatial distribution of industries in Great Britain: 2015, March 2017.
17 RF Analysis of Supply and Use tables, various.

would expect the UK to be one of those countries.[18] But the UK's pharmaceuticals have tilted towards supplying the UK's services industries since 2015, so, although our output has grown by 55 per cent, exports grew by just 7 per cent, slower than the average manufacturing sector. As a result, due to other countries' stronger exports and the UK's relative weakness, the UK no longer has a revealed comparative advantage in pharmaceuticals. Increasing output is valuable, but staying open to trade too is crucial for maintaining the sector's competitiveness, its role in global supply chains, and ensuring UK consumers benefit from a diverse supply of medicines.

FIGURE 3: **More than half of the goods in the UK economy are imported**

Supply of products by domestic, services imports and goods imports: UK, 2022



NOTES: Supply include domestic output at basic prices combined with imports. It excludes distributors' trading margins, and taxes less subsidies. Goods and services imports in domestic supply calculated using Leontief inverse.
SOURCE: RF analysis of Supply and Use tables, 2022; IOT tables, 2019.

And it isn't all about exports – we really need our goods imports. UK manufacturing is embedded in international supply chains and relies on inputs from all over the world. Goods imports directly comprise half of all goods products in the UK's economy, as shown in Figure 3. And when you take into account the supply chains that the UK is part of, including goods imports as inputs into domestic output, 60 per cent of goods in our economy are imported. This compares to 14 per cent of services products made from services imports.[19] These imports are both directly consumed by UK households and Government, as well as used as inputs into our goods production. So, the UK's recent weakness in goods imports is worrying.

18 RF Analysis of ONS, Annual Gross value added (GVA) by bespoke industry aggregations, Current price (CP) in GBP millions, November 2024. Revealed comparative advantage is calculated by comparing the share of a country's total exports in a specific good or service to the share of global exports in the same good or service.

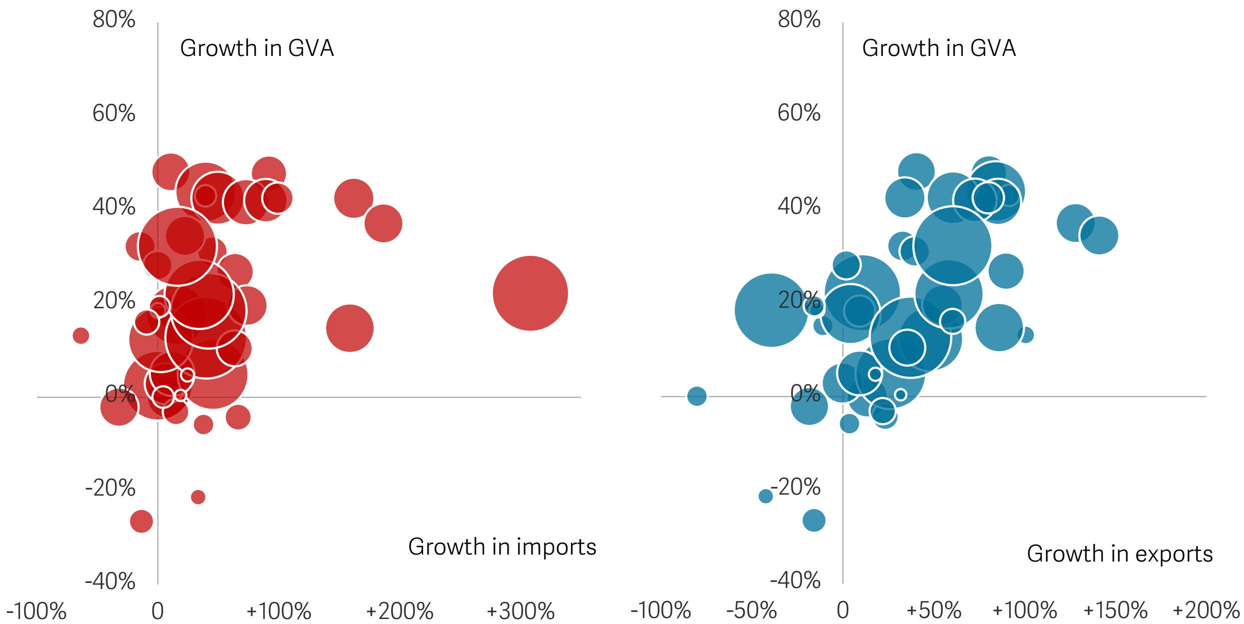
19 RF analysis of ONS, Supply and use tables, various. This rises to 64 per cent of goods and 17 per cent for services if both goods and services imports are taken into account.

Services trade has been much more robust

In the distant past, trade in services was something of an afterthought – they were described as 'invisibles' on the balance of payments.[20] Today, overseas service sales are central to Britain's growth prospects, and therefore the Government's ambitions to raise living standards. And although services as a whole remain less exposed to trade than goods, it now provides the majority – some 54 per cent – of UK exports.[21] Britain's mighty finance sector is actually today more export-intensive than manufacturing, and our professional services industries are equally open.[22] All this makes the UK a 'service superpower', selling more of them internationally than any other country except the US.

FIGURE 4: **Sterling services: UK trade has been more vibrant away from physical goods**

Import growth (left chart) and export growth (right chart) and GVA growth in services sectors: UK, 2015-2022



NOTES: Vertical line shows average growth in exports of 39 per cent. Horizontal line shows average growth in output of 18 per cent. Sectors without Services PPIs deflated using the average Services PPIs.
SOURCE: Analysis of ONS, Supply and Use tables, various; and ONS, Services PPIs.

Trade and output growth go hand in hand. Figure 4 illustrates this trend: services sectors with stronger output growth since 2015 have also expanded more rapidly in imports and exports. This relationship highlights how the UK's growing services sectors are benefiting from rising global demand of services. So expanding services trade is key to achieving the Government's ambitions for economic growth and rising living standards (see Box 1 for more details).

20 For example, the Bank of England described how invisibles had caused a deterioration in the UK's current account in 1960: Bank of England, Invisibles in the balance of payments Quarterly Bulletin, Q4 1961.
21 RF analysis of ONS, Trade Time Series, November 2024.
22 S Hale, Decent exposure: An overview of how Britain's exposure to trade has changed, Resolution Foundation, February 2024.

Trade and output growth go hand in hand. Figure 4 illustrates this trend: services sectors with stronger output growth since 2015 have also expanded more rapidly in imports and exports. This relationship highlights how the UK's growing services sectors are benefiting from rising global demand of services. So expanding services trade is key to achieving the Government's ambitions for economic growth and rising living standards (see Box 1 for more details).

Box 1: Who benefits from the growth of tradable services?

Those employed in tradable services are overrepresented at the top of the pay distribution, being 60 per cent more likely than the average worker to occupy roles in the 95th percentile of the wage distribution.[23] Meanwhile, workers in non-tradable services are most commonly employed at the bottom of the wage distribution. This suggests that a growth strategy based on boosting service exports might increase inequality.

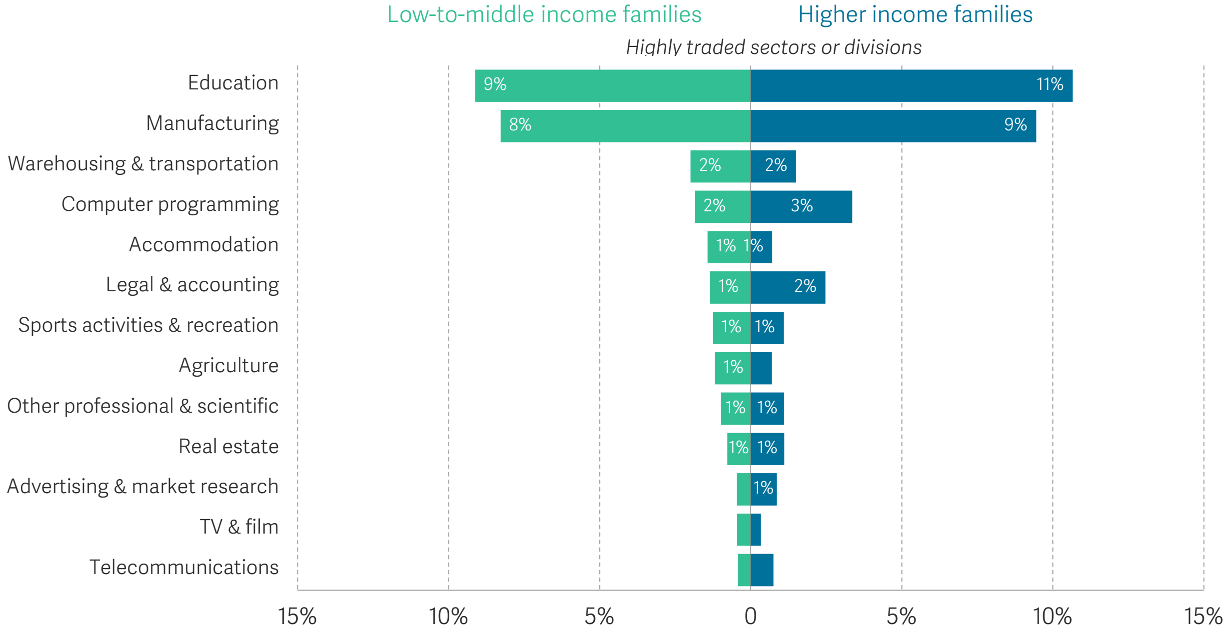
But this is too simplistic a conclusion. Higher wages in tradable services can drive demand for non-tradable services in local economies, particularly in the urban areas where services trade is concentrated.[24] The service trade (and spillovers from it) vary a good deal from place to place. Legal and accounting activities, for example, are clustered in London, while architectural and engineering services are concentrated in Tees Valley, Durham, and North Eastern Scotland. Scientific research and development, meanwhile, is anchored in Berkshire, Buckinghamshire, Oxfordshire, and the East of England.[25]

The sheer variety of tradable services means that growth can sometimes directly benefit lower earners. Certain export-exposed sectors shown in Figure 5 employ significant numbers of workers from low-to-middle income families. For example, education and warehousing activities provide jobs for 9 per cent and 2 per cent of all workers in low-to-middle-income families respectively.

23 J De Lyon, Enduring strengths: Analysing the UK's current and potential economic strengths, and what they mean for its economic strategy, at the start of the decisive decade, Resolution Foundation, April 2022.
24 E Fry & W Xue Barlow, Local roots of trade routes, Resolution Foundation, January 2024.
25 ONS, The spatial distribution of industries in Great Britain: 2015, March 2017.

FIGURE 6: **Some traded services, like Education, do support workers in poorer families**

Industry of those employed in highly traded sectors, by LMI/HI: UK, 2022-23



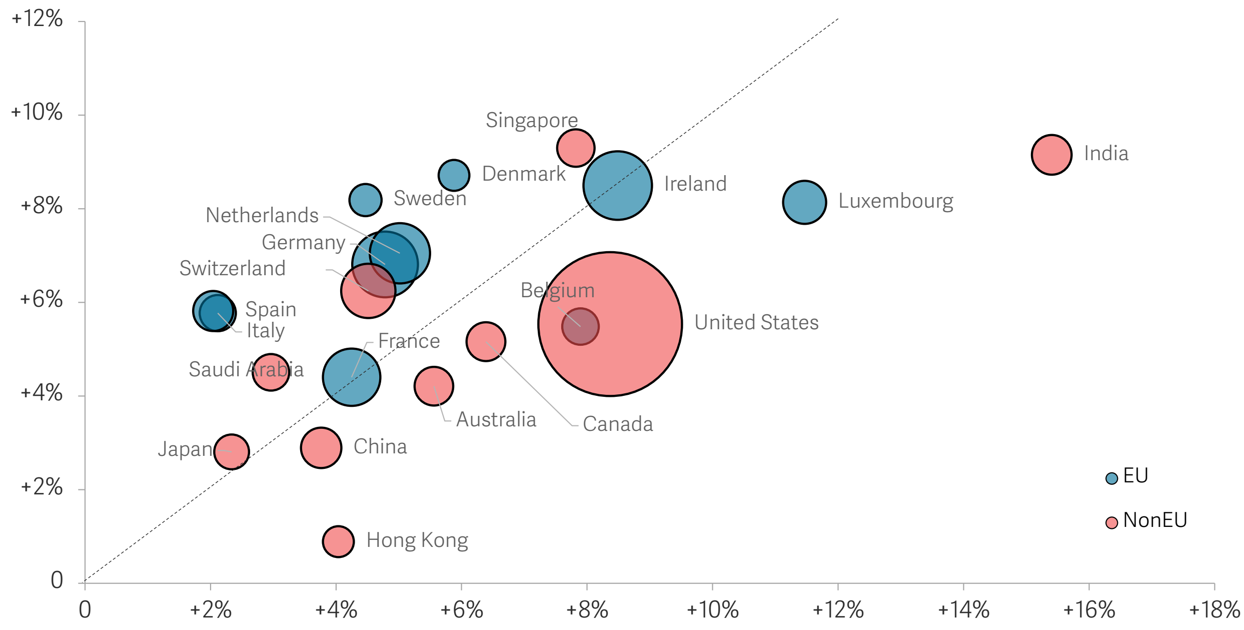
NOTES: Industry sector level shown for Manufacturing and Agriculture. All others are shown by industry division level.
SOURCE: RF analysis of ONS, Supply and use tables; and FRS.

The UK's established service strengths put us in a strong starting position

The UK has long been a global powerhouse in services, maintaining its position as the world's second-largest exporter of services in 2023. This strength is remarkably broad-based, spanning a range of sectors and trading partners. The EU remains the UK's largest trading partner, accounting for 36 per cent of UK services exports, but the US is close behind, buying 27 per cent of UK services. Switzerland is also a critical market, as shown in Figure 5. Since 2016, the UK has experienced growth across its major trading relationships, often outpacing the growth in these partners' imports from the wider world, for example the UK's services exports to India are up three-fold since 2016 (+215 per cent), while their imports from the world have doubled (+85 per cent). This shows that the UK is becoming an increasingly important supplier of services on the global stage.

FIGURE 6: **Service imports are growing internationally, and the UK is grabbing an increased share of this in key markets like the US and India**

Annualised growth in UK services exports (horizontal axis) and partner services imports from world (vertical axis): UK, World, 2016-2023



NOTES: Current prices. Countries chosen in the top decile of UK services exports by partner in 2023. Bubble size represents UK exports with partner in 2023.
SOURCES: RF analysis of UNCTAD, Exports by service-category

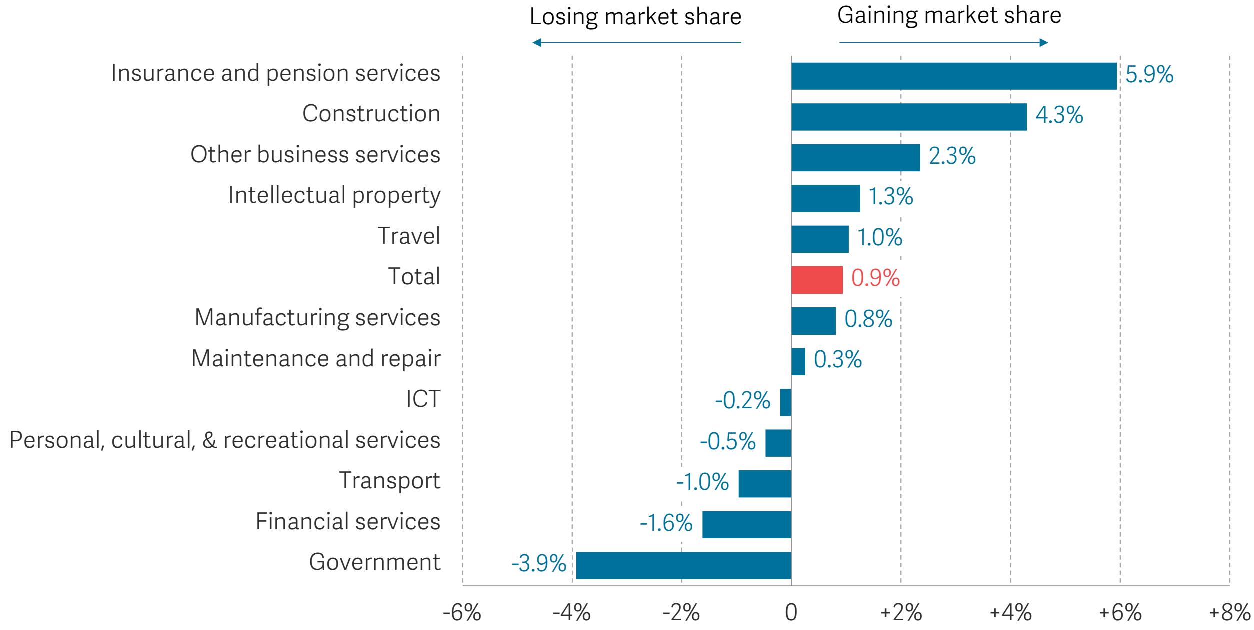
The UK's strengths span a wide range of sectors, with revealed comparative advantages in more than three-quarters of services sectors, including the five high-value services: 'other business services', financial services, insurance and pension services, intellectual property and telecoms.[26] Long-established pillars (eg finance, insurance and pension services) continue to underpin Britain's global position, while faster-growing areas like intellectual property further the success.

Overall, since 2019, the UK stands out in the OECD for having gained global market share in many important services. Britain's 'other business services' have stormed ahead, alongside insurance and pensions, and intellectual property gaining 2.3 percentage points, 5.9 percentage point, and 1.3 percentage points of market share among the OECD's exports to the world (Figure 7). The strength of these services means that the UK has increased its market share of total services exports by 0.9 percentage points of OECD sales, compared with France and the USA which lost 0.1 and 1.3 percentage points over the same period. Even when we consider the different sectoral compositions of countries, UK services exports have overperformed a typical OECD country since 2019.

26 RF analysis of UNCTAD, Exports by service-category & UN COMTRADE.

FIGURE 7: **Insurance, pensions and other business services have powered the boom in UK service exports**

Change in UK market share in services exports as a share of OECD's exports to the world: 2019 to 2023



SOURCES: RF analysis of UNCTAD, Exports by service-category.

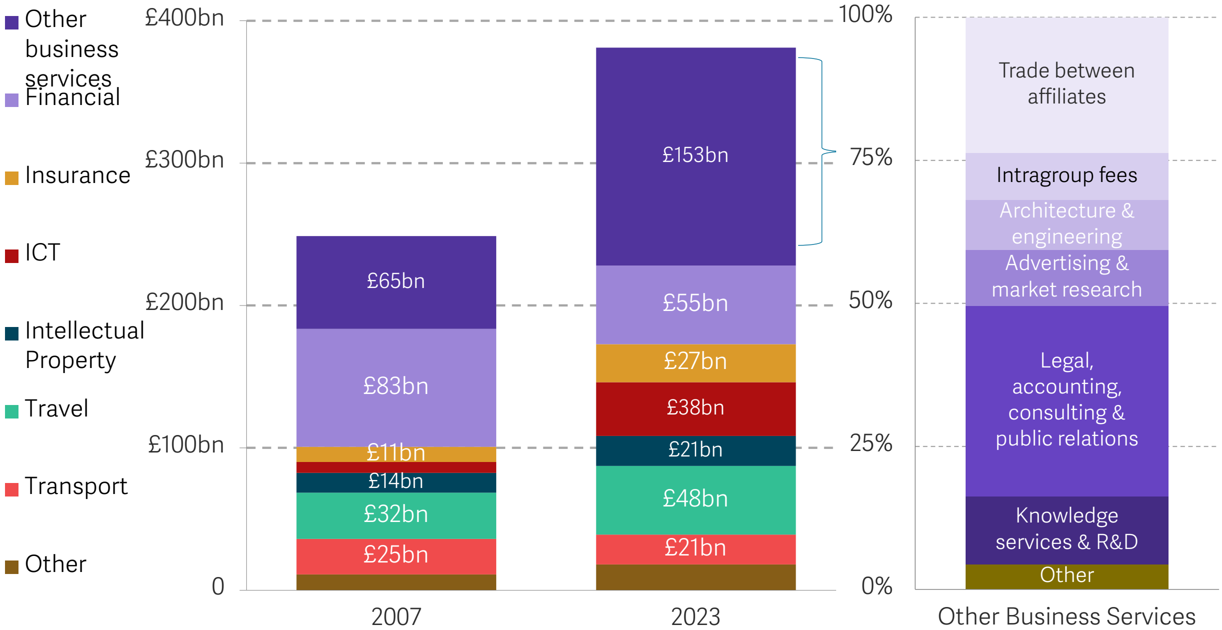
Openness to global demand can require a shifting sectoral mix, which has been evident in UK services since 2007. Back before the financial crisis, financial services were our largest export sector – 33 per cent of the total – it was just 15 per cent of the total in 2023. Information, communications and technology has gone from a standing start in 2007 – just 3 per cent of exports – to 10 per cent, reflecting the rapid growth in global demand over this period.

'Other business services' stand out as the UK's star performer, more than doubling in real terms and rising from 26 per cent of exports in 2007 to 40 per cent in 2023. This diverse category encompasses professional services such as 'knowledge services and R&D' (12 per cent), 'legal, accounting, consulting, and public relations' (33 per cent), as well as 'advertising and market research' (10 per cent) as shown in Figure 8. Additional significant components of 'other business services' suggest that it captures a substantial amount of activity and income closely tied to the operations of multinationals and the contemporary services trade: roughly a quarter of 'other business services' (around 24 per cent) relates to transactions between affiliates, with an additional 8 per cent accounted for by intra-group fees (Box 2).[27] These transactions have been growing rapidly.

27 'Intra-group fees' and 'trade through affiliates' both cover payments by affiliates to their parent companies for general management costs and reimbursements for expenses. These are on a balance of payments basis. For more detail on trade with affiliates, see Box 2.

FIGURE 8: **Other business services have powered recent growth**

Volume of UK services exports, by sector, and other business services broken down by product: UK



NOTES: Chained volume measures. 'Other' in total services exports includes Construction, Maintenance and Repair, Personal, Cultural and Recreational, and Government services. 'Other' in the right chart shows Other Business services categories: 'Other business services not included elsewhere', 'Other misc procurement', 'Trade related services', 'Operating leasing services', and 'waste treatment and de-pollution').
SOURCE: RF analysis of ONS 'Exports and Imports of Services by top level product accounts on CVM (chain volume measure) and CP (current price) Seasonally Adjusted basis.', £million

Four modes, two workarounds: the strategies that have kept UK services humming

One big difference between the goods and services trade is that, one way or another, goods always need to pass through a physical border. Sales in services, by contrast, can proceed through a whole variety of ways. The World Trade Organization's General Agreement on Trade in Services usefully distinguishes four different 'modes' of exchange. [28]

Mode 1 covers services delivered remotely (including those sold digitally); Mode 2 includes consumers traveling to another country for services like tourism or education; Mode 3 involves companies establishing a physical footprint overseas; and Mode 4 covers individuals temporarily providing services abroad. Finally, although not included in GATS, trade in services embedded in goods, such as design or engineering services, known as 'Mode 5' has been increasing over time.[29] Keeping these distinctions in mind helps navigate the complexities of global service trade, and the (not always consistent) way in which it shows up in the data. For example, Modes 1, 2, and 4 are usually captured

28 https://www.trade.gov/trade-guide-wto-gats, accessed 29 November 2024.
29 I Borchert et al., Links between services and manufacturing trade in the UK: Mode 5 and beyond, UK TPO, January 2022.

in balance of payments data, but Mode 3 may not be (See Box 2). And it turns out that Mode 3 – i.e. trading through subsidiaries – is especially important for making sense of the strategic international investments of countries like the UK.

During the period when Brexit was throwing up various new regulatory barriers to trading services, the UK nonetheless managed to outperform the OECD pack in global services markets by making heavy use of two of these modes of trade: the digital delivery of services (Mode 1) and supplying services via subsidiaries (Mode 3).[30]

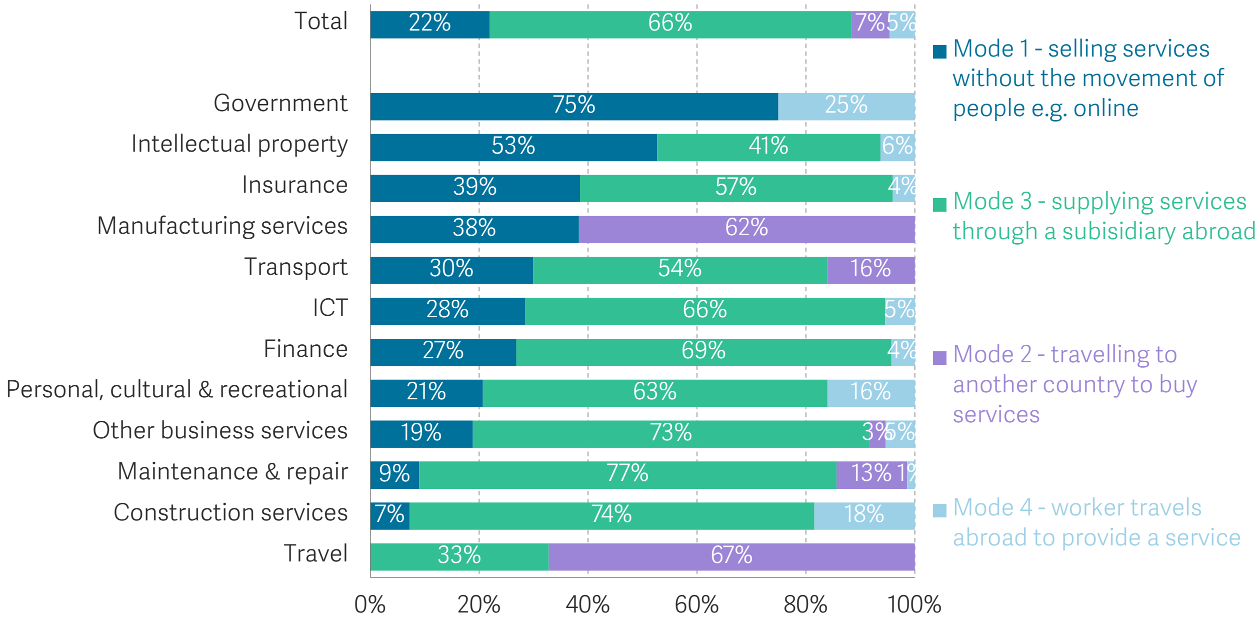
By 2019, these two strategies were already established ways of doing business. Back then, they together accounted for the vast majority of UK service sales overseas. As shown in Figure 9, 88 per cent of UK services supplied overseas were delivered through these two modes, far above traditional channels of selling services, such as workers traveling abroad to deliver a service (Mode 4) or tourists visiting the UK (Mode 2). [31] However, their deployment varied significantly by sector. For example, back in 2019, 19 per cent of other business services were delivered remotely, while 73 per cent were sold via subsidiaries (see Box 2 for a discussion of Mode 3 vs trade with affiliates). This left just 8 per cent conducted in person, either by workers travelling overseas or foreign clients visiting the UK. By contrast, only one-third (33 per cent) of travel services were sold by subsidiaries, with two-thirds (67 per cent) sold to tourists travelling to the UK to consume services. The fastest recent growth has often come in those fields – like 'other business services' and ICT – which were well-primed for the post-Brexit, post-pandemic world because they were already substantially organised around these two workarounds.

Increasing recourse to the digital channel, in particular, also made trading more efficient. Between 2000 and 2019, global trade costs for financial services, information and communication services and business services fell by between 30 per cent and 60 per cent. The surge in digital technologies – through the adoption of information and communication – has been found to be responsible for at least 25 per cent of the reduction in costs across these three sectors.[32] And this surge in digital trade has been particularly important for the UK, where the number of jobs embodied in digital services exports is as many as 3.2 million – compared to 1.8 million and 0.8 million in Germany and France respectively.[33] In a peculiar way, Brexit and the pandemic occurred at a good moment, as technology for digital sales – and the digital provision of services, such as video conferencing – was ripe for another step-change.

30 I Borchert, Services trade in the UK: What is at Stake?, UK TPO, 2016.
31 Here we discuss services supplied overseas as opposed to services exports. This includes subsidiaries which are owned in the UK, with a further discussion found in Box 2 on the different data reporting of trade and services supplied through subsidiaries. Estimates of Modes 1, 2 and 4 are derived from a balance of payments basis, but those of Mode 3 are derived using foreign affiliate statistics from 2018 and reported as experimental statistics. ONS, Trade in services by modes of supply, UK: 2019 , November 2020.
32 ICT was found to minimise operational costs and enable firms to bypass some services trade barriers. For more, see: S Benz, A Jaax & Y Yotov, Shedding light on the drivers of services tradability over two decades, OECD Library, October 2022.
33 S Benz, A Jaaz, & E van Lieshout, Digital trade and labour markets in the United Kingdom, 2024.

FIGURE 9: **How service sectors trade affects how much they trade**

Service types supplied by mode: UK, 2019



NOTES: Supply of services data on Mode 3 was derived by the ONS, combining data from 2018 outward foreign affiliate statistics with a trade in services by country and industry dataset as a country-industry-services correspondence table to link up data. The ONS doesn't report 'Mode 5' services trade – services which are embedded in manufactured goods. However, this is another important part of services sector trade.
SOURCE: Trade in services by modes of supply, UK: 2019.

BOX 2: **Trade between affiliated enterprises and Mode 3 trade**

In addition to selling services remotely and in person, companies can sell services through affiliated enterprises in another country. The ONS's International Trade in Services Survey (ITIS) captures 52 services 'products' including 'trade between affiliated enterprises'. This records intra-firm trade, such as payments by affiliates to their parent companies for "general management costs (for planning, organising and controlling) and reimbursements of expenses settled directly by parent companies, funds transferred by parent companies to affiliates for covering overhead expenses".[34] For example, a company in Manchester might charge its subsidiary in Paris a fee for use of its central HR systems. In the UK's trade data, this 'trade between affiliates' is counted as a subset of other business services (as shown in Figure 8), but the underlying activity that led to the value could

34 Eurostat, European Union international trade in services, Analytical aspects

have been generated by activity that could be in any sector. For example, an information services company, or a manufacturing service could be conducted using this services category (as shown by an alternative division of this data in Figure 11).

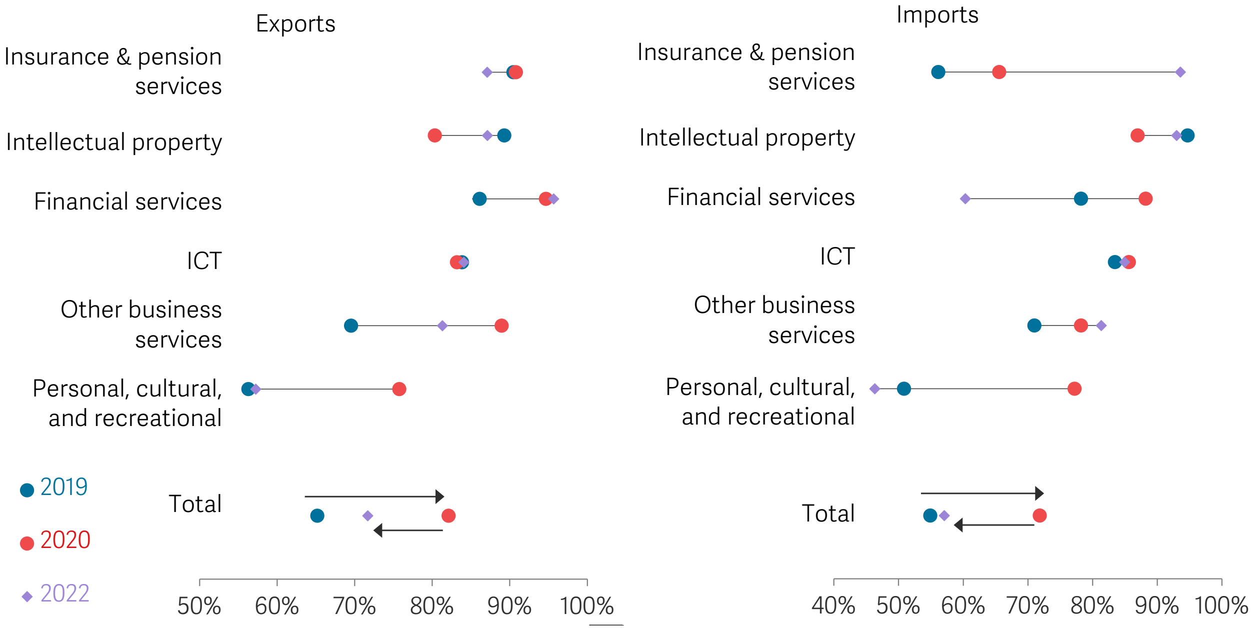
However, data recorded through the balance of payments offers a narrow perspective on the full scope of transactions and ownership structures within international subsidiaries. A broader view is captured under 'Mode 3' supply of services which records all UK-owned affiliate sales. To derive these, the ONS's foreign affiliate statistics are combined with trade in services by country and industry. This provides the overall picture of UK's business interests around the world.[35] Nonetheless, this method of services delivery carries risks, including lost turnover and tax revenue for the UK as profits are booked overseas as opposed to domestically.

Many companies confirm that the pandemic was a significant spur to change: almost a quarter of businesses who import (23 per cent) said they changed the way that they conducted international trade.[36] Globally, remote trading increased by nearly 40 per cent between 2019 and 2022, with services sold by temporary cross-border movement (Mode 4) dropping 60 per cent during the same period, and services sold via 'Mode 2' – typically tourism – also declining. [37] In the UK, sectors like business services, which started with relatively less remote trading (Mode 1), when measured as a share of in-person and remote delivery combined (Modes 1, 2, and 4), have increased their online trade. For example, the remote supply of other business services increased from 68 per cent in 2019 to 82 per cent in 2022 (Figure 10).[38]

35 ONS, Trade in services by modes of supply, UK: 2019 , November 2020.
36 RF analysis of ONS, UK Trade in services by modes of supply: 2020, February 2022 & ONS, Business Insights and Impacts on the UK Economy: Wave 49, January 2022 to February 2022. Figure includes all businesses excluding those with 0-9 employees who have imported in the past 12 months. Figure calculated as a share of those who import, as there is no question for whether a firm trades. This was 5.2 per cent of all businesses excluding those with less than 10 employees.
37 L Cernat, The big shift in global trade in services: a tale of five modes of supply, ECIPE, May 2024.
38 The sectors with the ability to pivot to digital trade are correlated with those sectors which are continuing to work from home – either hybrid or fully remotely – post-Covid. In December 2023, 77 per cent of information, communication and technology businesses and 60 per cent of professional services businesses operate either hybrid or fully remote working models, compared with 27 per cent of businesses overall. In comparison, just 11 per cent of transportation and storage businesses operate hybrid or fully remote work. ONS, Who are the hybrid workers? , November 2024.

FIGURE 10: **The digital bounce during the pandemic helped 'other business services'**

Services exports (left chart) and imports (right chart) by Mode 1 trade as a share of Mode 1, 2 & 4: UK



NOTES: Transport, Travel and Government are not included above as the allocation of modes of supply is based on Eurostat's proportional allocation of EBOPS categories to modes of supply, and so these do not change over time. This includes 'directly' delivered services trade, i.e. not delivered via subsidiaries. Mode 1 covers services delivered remotely (including those sold digitally); Mode 2 includes consumers traveling to another country for services like tourism or education; and Mode 4 covers individuals temporarily providing services abroad.
SOURCE: RF analysis of trade in services by modes of supply, UK: 2019; 2020, 2021 & 2022.

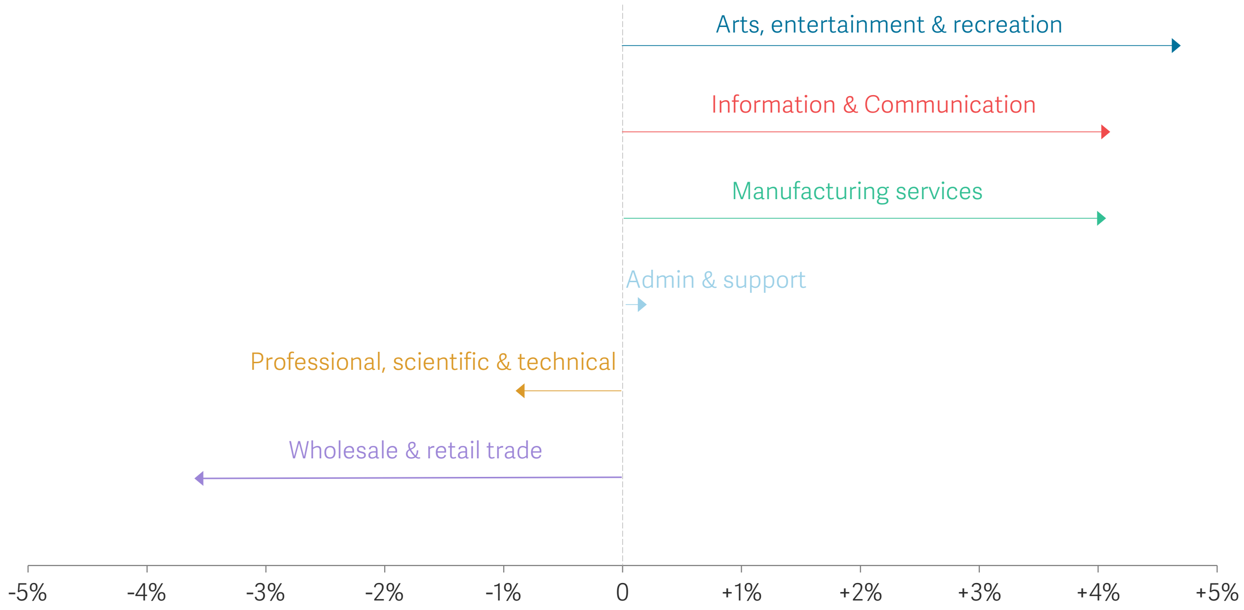
An increase in supplying services through subsidiaries

An even more significant workaround to services regulations involves companies setting up subsidiaries to trade in foreign markets. Some sectors ramped up the share of trade through affiliates after the Brexit referendum in 2016. For example, information and communication and manufacturing services (two large sectors) increased the share of trade between affiliated enterprises by 4.1 per cent and 4.0 per cent per year on average respectively in the post-referendum period compared with the pre-referendum period, controlling for both sector and year trends (Figure 11. A smaller sector – arts, entertainment and recreation – also saw a notable boost in trade between affiliates of 4.7 per cent per year after the referendum. Other sectors – such as professional, scientific and technical services – either couldn't or didn't adapt to the same extent.[39]

39 This aligns with other research which found that some types of professional services such as advertising and business management were able to trade through subsidiaries post-Brexit while others such as legal and engineering were less able to. For more discussion of this, see: H Breinlich & M Magli Should We Stay or Should We Go? Firms' Decision on Services Mode of Supply, CESifo Working Paper No. 11331, 2024.

FIGURE 11: **Information & communication is increasingly sold through subsidiaries**

Estimated percentage point change in share of value traded between related enterprises between 2010 to 2015 to 2016 to 2021: UK



NOTES: Triple-difference pooled regression. Tradeij,t=β0+β1(AffiliatesXPeriodXSector)+β2Year + β3Sector. Regression pools exports and imports. Standard errors clustered at sector level, with all coefficients significant at the 90 per cent confidence interval. Normalised by dividing the change by the level of trade by sector in the base years (2009 and 2016). Arts, entertainment & recreation is a small service sector.
SOURCE: RF analysis of ONS, International Trade in Services, various.

At a firm level, the switch to exporting through affiliates was more pronounced for EU compared with Non-EU partners. This suggests that firms were responding to anticipated and actual trade barriers related to Brexit, with certain sectors more, or less, able to 'mode switch'. [40] For example, information, communication and technology and computer services both experienced less disruption in overall trade flows due to their ability to mode-switch. However, sectors with lower potential for mode substitution, such as construction, faced more significant trade disruptions.[41] The increase in the share of exports to EU countries through affiliates has been found to be driven by firms starting to use affiliates more often, rather than expanding trade with existing subsidiaries.

Setting up a commercial presence, like a branch or subsidiary, helps maintain long-term trading relationships. While it requires significant upfront costs, it shows commitment to the market and allows businesses to navigate local regulations more effectively. Being on the ground helps build trust, adapt to changes, and stay competitive, especially in

40 H Breinlich & M Magli Should We Stay or Should We Go? Firms' Decision on Services Mode of Supply, CESifo Working Paper No. 11331, 2024.
41 H Breinlich & M Magli Should We Stay or Should We Go? Firms' Decision on Services Mode of Supply, CESifo Working Paper No. 11331, 2024.

markets where understanding local rules and customer needs is essential. So, the investments and trade through subsidiaries – particularly those in EU countries – should continue to sustain UK services trade for the sectors that can operate this way, perhaps acting as a complement as well as a substitute for services trade.

Where do these trade shifts leave the domestic economy?

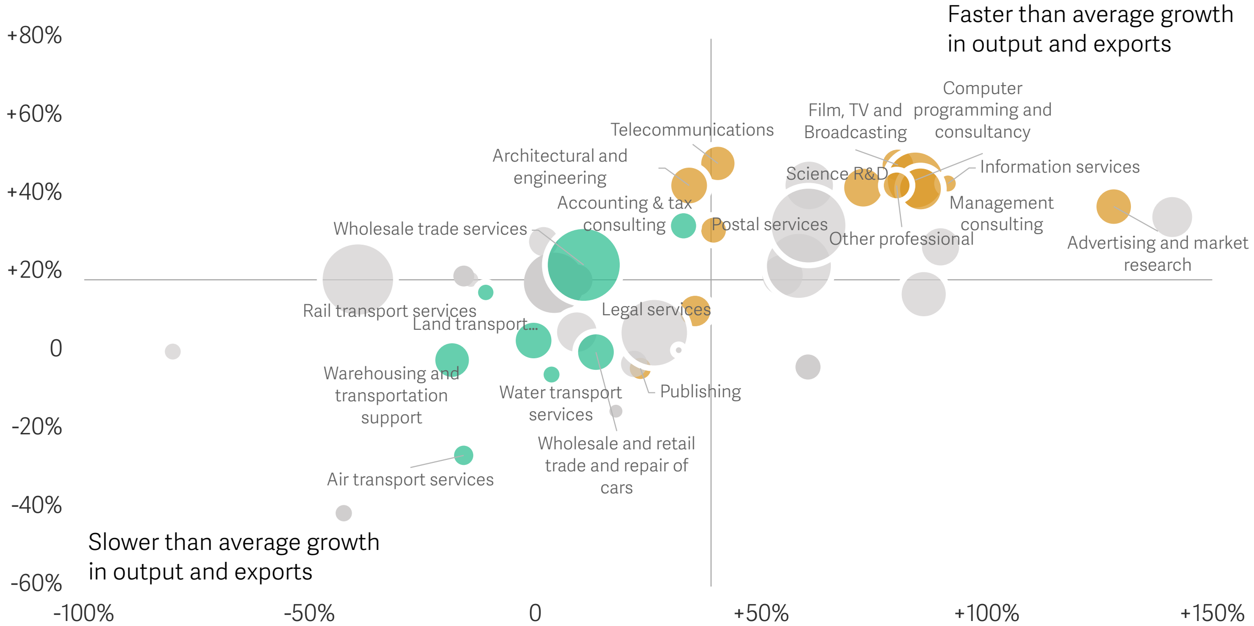
Both the introduction of trade barriers, and the variation in the ability of individual sectors to respond to these, are shaping the UK's economy. In particular, services output and exports have been storming ahead where domestic regulation isn't an issue or trade barriers are easier to circumvent. For example, sectors such as management consultancy, advertising and market research, and other professional services which are not subject to regulated professional qualifications, are growing quickly (Figure 12). Since 2015, management consultancy has grown 42 per cent in output and 85 per cent in exports, and advertising and market research has grown 37 percent in output since 2015, and more than doubled (growing 128 per cent) in exports. Although not formally regulated in terms of qualifications in the same way as fields like law, there are always general regulations which a local presence can help manage. For example, operating through subsidiaries in advertising and PR sectors has been key to navigating a set of haphazard regulations in different countries - London-based advertising giant WPP operates in over 100 countries through local subsidiaries.[42] Advertisers, while not requiring professional qualifications, must navigate distinct domestic regulations and cultural differences. In France, for example, influencers have been banned from promoting plastic surgery and gambling, and must clearly label sponsored content.[43] Subsidiaries help firms handle rules such as these, and comply with broader data and digital safety standards, which, though often voluntary, can carry steep fines for non-compliance.

It is common for firms in 'film, TV and broadcasting', 'computer programming' and 'information services' sectors – all part of the wider information, communication and technology sector – to set up subsidiaries, and use these to sell their services. These sectors have also performed well since 2015 – both in terms of exports and output. For example, the largest sector of these, 'computer programming and consultancy', has grown 84 per cent in exports and 44 per cent in output since 2015 (Figure 12).

42 WPP, Annual Report 2022, March 2023.
43 European Consumer Centre France, Influencers: obligations and responsibilities in Europe, May 2024.

FIGURE 12: **Qualified success: Regulated professional services have been growing more slowly than other services**

Export growth (horizontal axis) and output growth (vertical axis) relative to the average growth in selected sectors, bubbles sized by sector output: UK, 2015 - 2022



NOTES: Vertical line shows average growth in exports of 39 per cent. Horizontal line shows average growth in output of 18 per cent. Sectors without Services PPIs deflated using the average Services PPI.
SOURCE: RF Analysis of Supply and Use tables, various; ONS, Services Producer Price Indices (SPPI).

On the other hand, trade has struggled in areas where there is both complex regulation for UK firms to navigate and mode-switching is not an easy fix. Exports of highly regulated sectors – like accounting and tax consulting, engineering, and legal services – are growing slower than the average for services sectors overall. One issue for these sectors is the need for professionals to have their qualifications recognised in each EU country where they want to do business, a process that is often costly and slow. These slower growing services – accounting, engineering and legal – operate more through remote sales than through affiliates.[44] But, the extra bureaucracy post-Brexit is making supplying services remotely harder, limiting growth in these sectors.

In particular, financial services, a key export sector, has struggled since the Brexit referendum, with the UK losing market share among OECD countries since 2019: by 2023, exports were 33 per cent below their 2007 peak. A Swiss-style Mutual Recognition Agreement could ease trade barriers with key financial services partners, but no such deal currently exists with the EU or indeed other countries such as Japan or Australia, leaving firms to navigate tough barriers.[45]

44 H Breinlich & M Magli, Should We Stay or Should We Go? Firms' Decision on Services Mode of Supply, August 2024.
45 HM Treasury, The Berne Financial Services Agreement, December 2023; S Bhalotia et al., Trading Up: The role of the post-Brexit trade approach in the UK's economic strategy, June 2023.

Finally, transport services in the UK face additional challenges as a goods-related service sector, highlighting the interrelated nature of goods and services trade. Transportation and warehousing faces many of the same barriers as goods trade, including navigating customs and regulatory borders, border delays and checks, cabotage restrictions, and visa requirements for drivers. As Figure 12 illustrates, the sector has performed poorly in the post-Covid and Brexit era, with transportation and storage sector output rising just 1 per cent and exports falling by 8 per cent since 2015. And, as this sector employs more workers in low-and-middle income families than higher-income families, its decline will be particularly felt by low-income workers.

Looking ahead: reasons to be careful

While remotely supplying professional services has helped this particular sector during Covid, there are some signs of service customers becoming 'zoomed out' as in-person trade begins to rise again. As shown in Figure 10, the share of trade done remotely as a share of in-person and remote trade is slipping back into old habits. This is particularly the case for imports to the UK, for which remote supply as a share of direct sales (excluding subsidiaries) has fallen from a peak of 72 per cent in 2020 back to 57 per cent in 2022 (only slightly above 55 per cent in 2019), while UK exports have remained at 72 per cent remotely delivered in 2022 down from 82 per cent in 2020 (compared with 65 per cent in 2019).

Urging firms to trade through subsidiaries (or making it easier for them to take this route) doesn't come with zero costs to Britain. Firms more amenable to mode switching to foreign affiliate sales saw a decline of up to 0.3 per cent in domestic employment, as well as a small negative impact on firm turnover.[46] So while mode switching to trading through affiliates provides a flexible solution for companies in sectors able to do so, this type of trade is not as beneficial for domestic outcomes as remote or in person trade.

Taking a step back, the fact that certain services can mode switch suggests that services businesses can be more footloose than goods. If, for example, an ICT firm can easily set up a foreign affiliate when it faces new regulations that make exporting services in person harder, overall trade might not be affected much. But if switching modes is difficult, then new regulations could have a bigger impact on overall trade. This suggests that, for firms operating in specific sectors able to switch modes, effective barriers to trade in services might be somewhat lower than previously thought. It's also true that the UK, along with Japan and Spain, has the lowest average services trade restrictions in the OECD. But even with this relative leniency, and the ability of many sectors to switch modes, it remains true that across services as a whole, trade barriers remain high in contrast with goods.[47]

46 H Breinlich & M Magli, Should We Stay or Should We Go? Firms' Decision on Services Mode of Supply, August 2024.
47 OECD, Revitalising Services Trade for Global Growth: Evidence from Ten Years of Monitoring Services Trade Policies through the OECD STRI, OECD Publishing, Paris, 2024.

Finally, the weaker performance of warehousing and transportation is a reminder that goods and services trade are intertwined. But this interconnection extends to other sectors, such as advanced manufacturing (goods), which requires lots of software and after-sales support (services).

Implications for the Government's 2025 trade strategy

As the Government turns to crafting a trade strategy ahead of spring next year, it faces multiple difficult balancing acts. One important decision they have made is to tie the trade strategy to their industrial strategy, to 'overcome barriers and maximise trade' both in growth-driving sectors and across the broader economy, recognising that the markets that the UK has access to are important for the growth of key sectors.[48]

The Chancellor is right to aim to keep the doors open to 'free and open trade' with our most 'economically important partners'. [49] But the Government will need to carefully apportion diplomatic effort between negotiations affecting goods trade (where we have acute vulnerabilities and interests that can broadly be characterised as defensive) and services trade (the global sale of which look like Britain's best bet for the future). Striking the right balance here is a delicate task, even before considering the looming geopolitical challenges that Britain will be eager to avoid. The UK is already grappling with how to steer clear of an unwanted choice between trading with the US and the EU. Complicating matters further is a deeper dilemma: crafting a trade strategy that aligns its approach to goods with its ambitions for services.

How to avoid being forced to choose between goods and services

If goods were the only issue, the overriding strategy would be relatively clear: stay as open as possible as is consistent with holding your biggest trading partner close. That partner is still, overwhelmingly, the EU, from which we buy over half of all of our goods imports (£318 billion) and to whom we sell only a little less than half our goods exports (£186 billion) as shown in Figure 13.

This suggests that – considering goods trade in isolation – it makes sense to hold fast to EU standards, even if this could complicate or even reduce the (already low) chances of an attractive general US-UK Free Trade Agreement. As we have discussed elsewhere, the UK needs to balance a desire for regulatory autonomy with the growing costs of regulatory divergence – particularly in emerging regulatory areas such as climate and data.[50] Holding to EU standards is a way of stemming the damage from exiting the

48 Department for Business and Trade, Invest 2035: the UK's modern industrial strategy, October 2024.
49 HM Treasury, Mansion House 2024 speech, November 2024.
50 S Hale, EU-turn: Resetting the UK-EU relationship through strategic dynamic alignment, Resolution Foundation, October 2024.

Single Market and Customs Union, with big gains possible only by reconsidering the Government's red lines.[51]

FIGURE 13: **The EU still matters most for trading goods, but much less so for services**

Imports and exports by goods and services partner: UK, 2023

SOURCE: RF analysis of UK Total Trade By All Countries, Seasonally Adjusted, Q2 2024.

In addition to this, in the face of higher tariffs with the US, the UK needs to be pragmatic and grab any sector-specific deals the US offers as well as any agreements with countries elsewhere in the world that could be had without jeopardising that crucial cross-Channel relationship.[52] After all, we sell £60 billion of goods to the US each year and import £58 billion of their goods.[53] Modelling suggests that sectors with high US export exposure, such as pharmaceuticals, and those responsive to prices, such as fishing, could face the largest drops in exports to the US should Trump's tariffs be implemented.[54] And as tariffs loom, the UK should keep its mind on ways to dodge them – after all, it is unlikely that any new tariffs will be as universally applied as they have been proposed; large companies will undoubtedly be lobbying for exemptions.[55]

51 S Bhalotia et al., Trading Up: The role of the post-Brexit trade approach in the UK's economic strategy, June 2023.
52 S Keynes, How to dodge a tariff, Financial Times, 15th November 2024.
53 Trade asymmetries are common in international trade data and appear in UK-US goods trade. The UK thinks we have a small surplus in goods trade in 2023, while the US thinks they have a small surplus in goods trade.
54 N Tamberi, Will Trump impose his tariffs? They could reduce the UK's exports by £22 billion, UK Trade Policy Observatory, November 2024.
55 D Hening, How Trump affects UK Trade Policy , UK TPO, November 2024.

But even if goods were the only consideration, the imposition of new tariffs would not only knock goods exports to the US, but also complicate the strategic calculation. For the UK in isolation, the least-bad option might be living with some of these tariffs, while being selective about retaliation, so that Britain's businesses and consumers could continue to benefit from US imports and stem the damage from imports from the rest of the world.

In a world of rising trade tension, however, such unilateral openness could be hard to sustain if the EU became anxious about the UK being a backdoor for goods from the US and beyond. The UK has already taken a very different stance towards China's electric vehicles (EVs) than either the US or the EU, by continuing to allow them in with its (relatively modest) existing 10 per cent tariff compared with up to 45 per cent for China EV imports to the EU and up to 100 per cent for China EV imports to the US.[56] We sell £31 billion of goods to Canada, China and Mexico – the three countries in the eye of Trump's trade tariffs – and import £63 billion from these countries. Should these countries be impacted by Trump's tariffs, the UK might be a beneficiary if these exports divert to the UK but this will need to be weighed up against the risks to our exports as these markets potentially lose key business with the US. If we were to take American goods tariff-free in an environment where the EU were retaliating to US tariffs, Brussels may worry about US imports being diverted through the UK to try and avoid being caught. This is a reminder that, as a medium-sized country dependent on a nearby giant market for trading goods, there are limits to the scope for the UK to act independently.

Services must be the priority in the Government's trade strategy

So there is a potential conundrum even before we get to services, where UK interests are much more expansive and varied than is the case with goods. Our analysis points to a host of important objectives for policy, including: keeping those crucial 'workarounds' running smoothly, staying alert to tensions around the regulation and taxation of subsidiaries and digital sales, and maintaining a functional global data regime.[57] While a slowdown in the growth in trade between affiliates in 2024 might reflect a new normal level of trade between subsidiaries post-Brexit, we need to make sure that the ability to move to trading through subsidiaries continues to be open for services which can trade this way – notably ICT, certain professional services, and manufacturing services. Meanwhile, Britain should target digital agreements more widely to enable growth in 'other business services' sectors in particular. For example, the UK should leverage the continuation of the WTO e-commerce moratorium agreed in early 2024 which ensures

56 A Corlett, Z Leather & J Marshall, Getting the green light: The path to a fair transition for the transport sector, Resolution Foundation, October 2024.

57 For a discussion on the fragmentation of global digital economy governance, and potential ways forward, see: J Cacchus et al., Interoperability of Data Governance Regimes: Challenges for Digital Trade Policy, CITP, April 2024.

that the current practice of not applying tariffs to electronic transmissions continues.[58] Meanwhile, Britain can focus on locking in data adequacy to facilitate the transfer of data, as well as provisions on electronic authentication and digital identity approaches through digital agreements.

Given the relative underperformance in regulated services, which have lagged their unregulated counterparts, perhaps facing challenges with mode switching, a serious effort is needed to ensure that they can fully participate in Britain's service export boom. Brokering mutual recognition agreements for professional qualifications in sectors such as legal services, architecture, engineering, accounting and publishing should be a priority. These agreements are vital for enabling professionals to operate seamlessly across borders – a task that cannot be left to the private sector alone. And, although Europe remains an important focus for these agreements, the UK must also prioritise its high-risk, high-reward FTAs with large, growing markets like India, as well as deeper service agreements with countries with regulatory frameworks closely aligned to its own, such as Australia, Singapore, and Switzerland.[59] Special attention must also be given to the US, a critical market that already accounts for about a quarter of the UK's service exports. Expanding access to these markets will not only boost Britain's trade but also enhance its global competitiveness in high-value, regulated sectors.

Fortunately, some of the most testing aspects of goods trade – hard borders, physical checks, and concerns over 'backdoor' access – don't apply in quite the same way to services. Nor does the trade in services face the intense political scrutiny that Trump is directing towards merchandise trade. However, there is considerable unease that Britain might be forced to 'choose' between America and Europe. But we should reject this dichotomy: the UK must adopt a global outlook, seeking opportunities for service trade agreements wherever they arise, and remaining pragmatic about the diverse, and often technical and unglamorous, routes to progress.

Even more critical than navigating rival trade blocs is avoiding a false choice between defending goods trade in the threat of a return to protectionism, something that would be essential to the UK's current economic stability, and advancing the trade in services, which represents Britain's brightest prospect for future growth. While it may not capture headlines, ensuring services thrive will be key to Britain's long-term success.

58 A Andrenelli & J López González, Understanding the scope, definition, and impact of the WTO e-commerce moratorium, VoxEU, March 2024.

59 The Rt Hon Sir Keir Starmer KCB KC MP, Prime Minister announces relaunch of UK-India free trade talks, November 2024; S Bhalotia et al., Trading Up: The role of the post-Brexit trade approach in the UK's economic strategy, June 2023.

The Resolution Foundation is an independent research and policy organisation. Our goal is to improve the lives of people with low to middle incomes by delivering change in areas where they are currently disadvantaged.

We do this by undertaking research and analysis to understand the challenges facing people on a low to middle income, developing practical and effective policy proposals; and engaging with policy makers and stakeholders to influence decision-making and bring about change.

For more information on this report, contact:

Emily Fry
Senior Economist
Emily.Fry@resolutionfoundation.org

Resolution Foundation

2 Queen Anne's Gate
London SW1H 9AA

Charity Number: 1114839

@resfoundation
@resfoundation.bsky.social
resolutionfoundation.org/publications