CPD Working Paper 121

BREXIT and Bangladesh
An Exploratory Study on Likely Economic Implications

Mustafizur Rahman
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The present paper titled **BREXIT and Bangladesh: An Exploratory Study on Likely Economic Implications** has been prepared under the Independent Review of Bangladesh's Development (IRBD) programme of the CPD. The paper is authored by *Professor Mustafizur Rahman*, Distinguished Fellow, CPD <mustafiz@cpd.org.bd>; *Mr Towfiqul Islam Khan*, Senior Research Fellow, CPD <towfiq@cpd.org.bd> and *Ms Sherajum Monira Farin*, Research Associate, CPD <sherajum@cpd.org.bd>

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Abstract

UK's EU-referendum held on 23 June 2016, and the verdict of the British electorate to leave the EU (popularly known as *Brexit*), have important implications not only for the UK, but also for its major trading and economic partners, both within and outside of the EU region. This paper aims to capture the possible short- and medium-term implications of Brexit for the economy of Bangladesh. The paper makes an attempt to anticipate the terms of Brexit, and what these could mean for Bangladesh's bilateral economic relationship with the UK in a diverse range of areas. With the help of a gravity model exercise, the paper tries to capture the likely fallouts of Brexit on exports of Bangladesh to the UK. The paper argues that Bangladesh's exports, remittances, FDI and aid could be significantly affected by Brexit. The paper comes up with a number of recommendations to address the likely challenges facing the Bangladesh economy arising out of Brexit.

Contents

Acronyms

ADB	Asian Development Bank
BCA	Bangladesh Caterers Association
BDT	Bangladeshi Taka
CETA	(EU-Canada) Comprehensive Economic and Trade Agreement
CNY	Chinese Yuan
CPI	Consumer Price Index
DAC	Development Assistance Committee
DF-QF	Duty-free Quota-free
EBA	Everything But Arms
EC	European Council
ECA	European Communities Act
EEA	European Economic Area
EFTA	European Free Trade Area
EIB	European Investment Bank
EU	European Union
EUR	Euro
FDI	Foreign Direct Investment
FEM	Fixed Effects Model
FTA	Free Trade Agreement
FTSE	Financial Times Stock Exchange
GBP	British Pound
GDP	Gross Domestic Product
GNI	Gross National Income
GSP	Generalised Scheme of Preferences
G8	Group of Eight
G20	Group of Twenty
HS	Harmonised System (of coding)
IMF	International Monetary Fund
INR	Indian Rupee
IPR	Intellectual Property Rights
LCU	Local Currency Unit
LDC	Least Developed Country
LMIC	Lower Middle-Income Country
LSDV	Least Square Dummy Variable (model)
MFN	Most Favoured Nation
MP	Member of Parliament
NGO	Non-Government Organisation
NIESR	National Institute of Economic and Social Research
NTB	Non-Tariff Barrier
ODA	Official Development Assistance
ODI	Overseas Development Institute

OECD	Organisation for Economic Co-operation and Development
OLS	Ordinary Least Squares (regression)
ONS	Office for National Statistics (UK)
PPML	Poisson Pseudo Maximum Likelihood (estimation)
REM	Random Effects Model
RMG	Readymade Garments
RoO	Rules of Origin
SEZ	Special Economic Zone
SPS	Sanitary and Phytosanitary
TBT	Technical Barrier to Trade
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
USA	United States of America
USD	United States Dollar
VND	Vietnamese Dong
WTO	World Trade Organization

1. INTRODUCTION

The British electorate's decision to leave the European Union (EU), popularly known as Brexit, was likely to have far-reaching consequences, going beyond the borders of the United Kingdom (UK) and the EU. Brexit will undoubtedly pose significant economic, political and geo-political implications at various levels—UK domestic, EU-wide, as well as global. In the context of this evolving scenario, it is important that developing countries such as Bangladesh remain informed and alert about the developments following the Brexit. It is pertinent to recall here that, Bangladesh maintains a diverse range of economic relationships both with the UK and the rest-EU. Thus, the overall impact of Brexit for Bangladesh will be both direct, through interfaces of the Bangladesh economy with the UK economy; and indirect, owing to the EU-wide and global impacts that could have potential implications for the Bangladesh economy. Though to what extent Brexit will affect the Bangladesh economy still remains unclear, and will depend on the terms of separation of the UK from the EU, Bangladesh should invest in developing early preparedness and a suitable response strategy because of several reasons. First, Brexit is a new phenomenon; therefore, how the negotiations will proceed and end, is difficult to anticipate; second, it is to be seen how UK's position unfolds in the course of negotiations; third, how key EU countries, European Commission and Council will come up with their own proposals in view of UK's negotiation also need to be observed.

Some of the signals are already emerging, particularly in the backdrop of the debates that have taken place in the UK Parliament, statements by the UK Government, and in the context of the ongoing UK-EU discussions. The White Paper titled "The United Kingdom's exit from and new partnership with the European Union" published by UK's newly set up Department for Exiting the European Union, on 2 February 2017, articulates the principles and key negotiating stance of the UK, and also the non-negotiables, in broad terms. The White Paper has made it clear, that the UK will not be seeking membership of the 'Single Market', but instead will pursue a new 'strategic partnership with the EU including an ambitious and comprehensive free trade'.[1] This, along with the focus on controlling immigration to the UK—are issues of heightened importance to Bangladesh. Already the fault lines have been drawn—EU has cautioned, that they would not allow UK to 'cherry pick' while leaving the Single Market (The Economist, 2018).

As is known, Bangladesh is a key beneficiary of the preferential treatment under the EU's Everything But Arms (EBA) arrangement by virtue of being a least developed country (LDC). However, in a welcome development, the UK Government has announced, that it will allow Bangladesh to retain this benefit even after Brexit. This was informed through a press release on 24 June 2017 (Department for International Development and Department for International Trade, Government of UK, 2017). Nonetheless, since Bangladesh has gained eligibility for LDC graduation in March 2018, to finally graduate in 2024, it will need to prepare for the time when Bangladeshi goods will not enjoy duty-free market access in the UK. Additionally, although EU had offered continuation of duty-free access to LDCs for another three years after graduation (for Bangladesh this will be till 2027), UK has not made any such commitment. Brexit will have important implications for UK and the EU, and also for the countries which do business with them. It is from this vantage point, that the present study, which explores the possible implications of the Brexit for the Bangladesh economy, has relevance and importance.

The motivation of the study is to initiate an informed discussion in Bangladesh, so that the key stakeholders including policymakers, business and private sectors, producers and consumer groups,

[1]The Single Market refers to the EU as one territory without any internal borders or other regulatory obstacles to the free movement of goods and services (European Commission, 2018a). The Government of UK has published its plan for 'a new, positive and constructive' partnership in the mutual interest of the UK and the EU, with a White Paper presented to the Parliament on 2 February 2017 (Department for Exiting the European Union, 2017).

and development partners are made aware of the potential implications of Brexit and the necessary steps Bangladesh should take in this regard. The objective of the study is to identify the transmission routes of Brexit's impact on the Bangladesh economy, capture impacts, and suggest measures to address the possible consequences.

2. THE BACKDROP: THE EU-REFERENDUM AND BREXIT NEGOTIATIONS

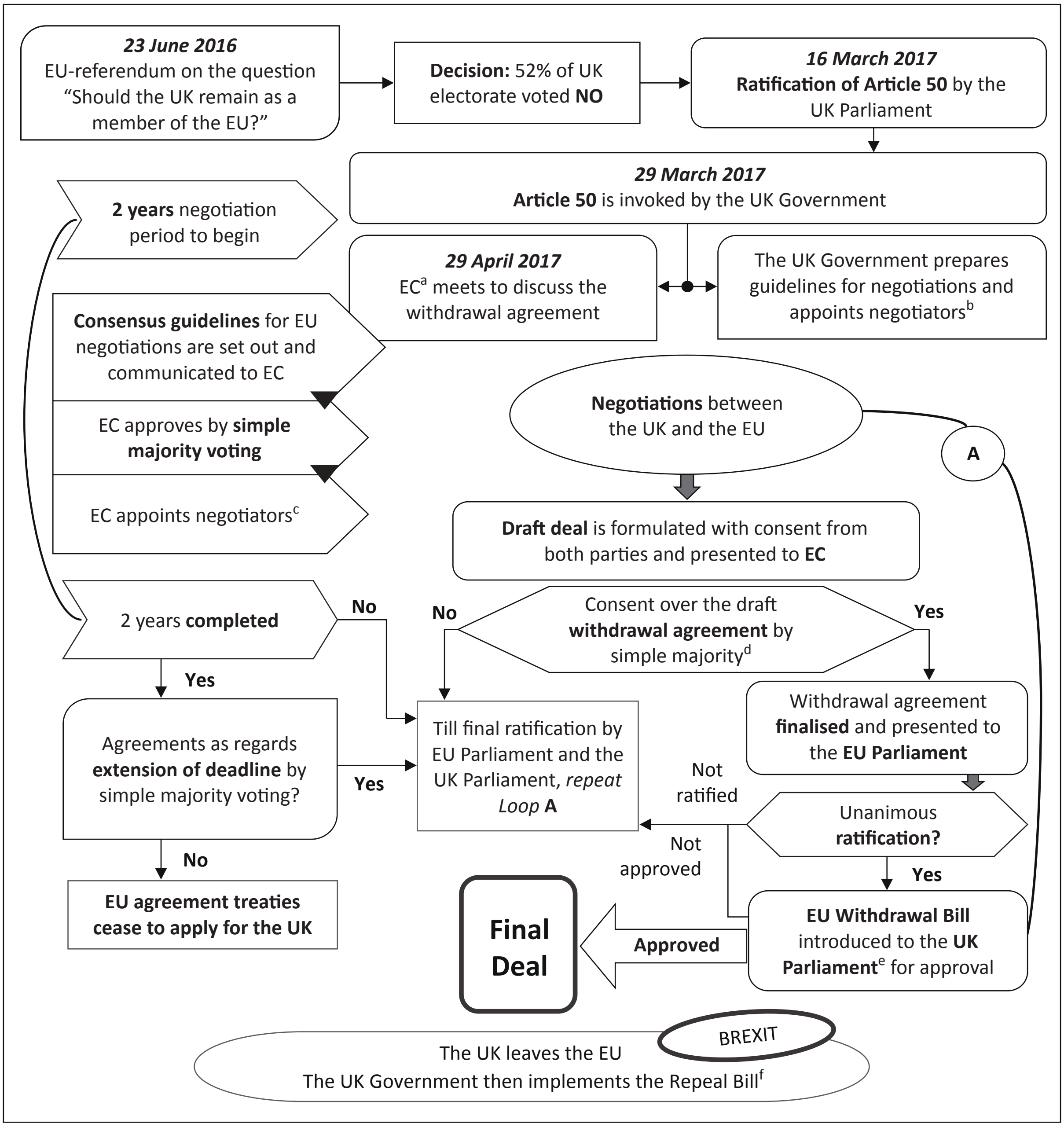
The debate as regards whether the UK should continue to stay in the EU or not, was brewing for quite some time. Whilst the political leaders of the two major parties in the UK were interested in the country remaining in the EU, strong opposition from some of the key leaders, particularly in the ruling Conservative Party, forced the (then) Prime Minister, David Cameron, to promise a referendum on Brexit if Conservatives were reelected. The referendum was set to be held on 23 June 2016. Cameron was criticised on the ground, that this had more to do with appeasing the anti-EU Conservatives than empowering the public, since he had earlier rejected holding such referendum in 2012 during his first term (Iyenger, 2016). Cameron himself supported 'Britain Stronger in Europe' campaign which was a key slogan of the 'Remain' side. Remain was opposed by the 'Vote Leave' campaign, whose aim was to 'free Britain from the Brussels rule'. The campaign had set off on 15 April 2016. Campaigners from both Remain and Leave sides made claims (though not always factually correct[2]) in support of their respective stances. Key arguments, in this connection, are presented in the Annex 1 (see Annex Table 1). It is observed that, the Remain supporters presented strong evidence on economic advantages emanating from remaining in Europe, while the Leave campaigners harped more on emotional issues, such as regaining UK's sovereignty and taking back control of such important issues as migration from bureaucrats in Brussels. In the end, the Leave received 51.9 per cent of the vote against 48.1 per cent for the Remain. Nation-wise disaggregation showed that England and Wales had voted to leave, whereas Northern Ireland and Scotland had voted to remain in the EU (Annex Figure 1).

Brexit negotiations are proving to be complex and protracted. Article 50 of the Lisbon Treaty establishing the EU was introduced in 2009 to empower member states with a notification mechanism in case it was no more willing to stay in the EU. For the first time on 29 March 2017, Article 50 was evoked by the UK Government. A roadmap of the process that was to be followed subsequent to invoking Article 50 is presented in Flowchart 1. The series of significant events which preceded and followed the EU-referendum is highlighted in the Annex 2. According to the rules, the timeline to complete the process of withdrawal from the EU is two years from the date on which Article 50 is invoked. However, the time may be extended, subject to mutual consent. The EU has come up with a proposal for a transition period for the UK, after Brexit has happened, which extends up to 31 December 2020.

To develop an understanding of the possible deals that the UK can make with the EU, the current architecture as regards the various arrangements within the EU has been reviewed. The existing relationship between UK and the EU is quite special—it allows the former to access the EU Single Market without being obliged to join the Eurozone or the Schengen border-free area. Following Brexit, the UK will be required to explore options for the post-withdrawal relationship with the EU and other EU member countries. There were several options that could emerge in the course of the negotiations: be a non-EU member of the European Economic Area (EEA), an arrangement similar to Norway or as a member of the European Free Trade Area (EFTA) such as Switzerland; UK can also opt for the Turkish-style Customs Union Agreement or Free Trade Agreement (FTA) with the EU such as the EU-Canada Comprehensive Economic and Trade Agreement (CETA). The other option, which is a default option, is

[2]Remain campaigner David Cameron's claim that leaving the EU would levy a cost of GBP 4,300 per household was later dismissed by Britain's fact-checking authority. Similarly, the claim made by Leave campaigners Boris Johnson and Nigel Farage that the EU membership costs Britain GBP 350 million per week was proved to be wrong by the UK Statistics Authority (Payne, 2016).

Flowchart 1: Likely Sequence of Events Following the Onset of Article 50



Source: Prepared by the authors based on information provided in Department for Exiting the European Union (n.d.); European Council (n.d.); Hunt and Wheeler (2018).

Note: [a] EC, in all cases of this Flowchart, refers to the European Council with heads of the 27 EU member countries, excluding that of UK, in the context of Brexit.

[b] UK negotiators were (initially) David Davis, Oliver Robbins, Tim Barrow and Sarah Healey.

[c] EU negotiators included Michel Barnier, Sabine Weyand, Donald Tusk and Didier Seeuws.

[d] Simple majority voting establishes that an agreement will come into force if at least 20 member countries with 65 per cent of the EU-population approve the agreement.

[e] Once the UK and the EU finalise the withdrawal agreement, UK will introduce the EU Withdrawal Bill to revoke the 1972 European Communities Act (ECA).

[f] The Repeal Bill will incorporate the existing EU laws into UK laws. The process of amending and upgrading the laws as per the UK's needs will be initiated. This will give the UK business and economy time to adjust to the newly emerging scenario.

like the most favoured nation (MFN) type of agreement in the World Trade Organization (WTO), which comes with no special deal. These possible scenarios are elaborated in Box 1.

Box 1: Potential Scenarios that could Emerge Following the Brexit Negotiations[a]

Potential Scenario	Arrangement and Obligation	Comment
Norway-type arrangement	• Non-EU EEA[b] member • Significant access to the EU Single Market[c] • Exports have to satisfy rules of origin (RoO) requirements • High 'passporting rights', but not full[d] • Makes significant contribution to the EU spending • Is a signatory of the Schengen Agreement • Norwegian laws incorporate approximately 75 per cent of EU-laws[e] • Has a limited vote or veto power (only via some formal engagement) in the formation of the EU rules and regulations	Fails to secure independence of courts, freedom to strike new trade deals and limit immigration—the drivers of Leave campaign
Switzerland-EU bilateral approach	• Switzerland is a member of the EFTA[f] • Has bilateral treaty arrangements with the EU, which allow flexibility in choosing particular EU initiatives in which it is willing to participate • Moderate level of market access (lower than Norway) to the EU Single Market • Does not have 'passporting rights' • As is the case with Norway, Switzerland has to contribute to EU spending and allow free movement of people under Schengen Agreement • Switzerland is obliged to adhere to a significant share of the EU-obligations, but has no say as regards their design and formulation	Relatively attractive for the UK, but not of much appeal to the EU
Turkish-style Customs Union Agreement	• The EU is in a customs union with Andorra, Monaco, San Marino and Turkey through agreements which do not offer complete sectoral coverage. For instance, the EU-Turkey Customs Union is applicable only for industrial goods, and does not cover important economic areas such as agriculture, services and public procurement • There is no internal tariff within the countries • UK, if in a customs union agreement, will have to apply EU external tariffs and will need to abide by the EU product market regulations without influence or guaranteed access to third markets	This may not be a preferred option for the UK, as market access to EU will be partial—UK can work for a more closely tied arrangement
Free Trade Agreement (FTA)	• UK will be free to negotiate FTAs independently with current trading partners including the EU • Tariff barriers are unlikely under this scenario; however, non-tariff barriers (NTBs) are likely to surface. For example, under the EU-CETA[g], many Canadian exports are subject to standard requirements which were set and imposed by the EU • No guaranteed full access to the Single Market	A possible option that may prove to be beneficial for the UK
No agreement or WTO-MFN arrangement	• Under this scenario the UK-EU trade is governed by the WTO regulations, i.e. the UK's exports to the EU and other WTO members will be subject to importing countries' MFN tariffs. The UK is likely to lose competitive advantage • UK will lose preferential access to the EU Single Market • All the EU trade agreements will cease to apply for the UK, thus generating the need to negotiate new trade deals with over 50 countries • UK will have full freedom to negotiate a new immigration policy, and will no longer be obligated to adhere to the EU rules	This will be the most disruptive and conservative case. Both the UK and EU markets will be significantly affected

Source: Authors' compilation based on information provided in IMF (2016b); World Bank (2016); GOV.UK (n.d.a); European Commission (n.d.a).

Note: [a] Possible arrangements with the EU are presented in descending order of economic integration and increasing order of political flexibility.

[b] EEA comprises of Iceland, Liechtenstein and Norway with the EU.

[c] EEA-type arrangement will provide partial access to the EU Single Market (lower than that available under EU membership). The EEA agreement does not cover agriculture or fisheries, and non-EU EEA countries are outside the customs union which means that these are open to non-tariff barriers (NTBs) such as rules of origin (RoO) requirement and trade rules such as anti-dumping duties.

[d] EEA membership would confer 'passporting rights' to banks and insurers.

[e] Calculated by an independent study commissioned by the Norwegian Government (2012).
[f] EFTA is an intergovernmental organisation set up for the promotion of free trade and economic integration between its four member states—Iceland, Liechtenstein, Norway and Switzerland.
[g] The CETA (between EU and Canada) is a freshly negotiated trade arrangement which is yet to be put in place. However, arrangements similar to CETA would not be much appealing to the UK, since it does not give Canada access to the EU Single Market in important areas like air travel, broadcasting and banking. Moreover, Canadian manufacturers exporting to the EU are subject to a range of bureaucratic costs, and many agricultural exports are subject to quotas and tariffs.

The 'Norway' scenario will offer the least disruption in terms of trade and investment consequences, and thus, can also be termed as 'Soft Brexit'. However, this may not serve the UK Government's political objective to break free of the EU regulations. On the other hand, going on the path of 'Hard Brexit' would mean opting for a WTO-MFN scenario which offers maximum level of control over immigration policies, trade deals and overall economic decision-making, but this will also involve high costs and uncertainties (Global Counsel, 2015; Dhingra *et al*., 2016; World Bank, 2016). From a hierarchical perspective, the Norway scenario is better than the FTA scenario, which is better than the MFN scenario which offers the least economic integration. It is understood from the 'current' discourse in the UK governing circle that the two extremes—Norway-EEA scenario and the WTO-MFN scenario—are both unlikely.[3]

Another viable arrangement, as proposed by the opposition Labour Party leader, Jeremy Corbyn, is pursuing the policy of remaining within the customs union with EU after Brexit.[4] Confederation of British Industry has supported this stance. Although by voting for Brexit, the UK has voted to leave the existing customs union, this does not preclude the possibility of forming 'a new customs union' with the EU. Andorra, Monaco, San Marino and Turkey have this type of arrangement with the EU (Box 1).[5] As distinct from an FTA, a customs union does not only abolish tariffs and quota for members, it also stipulates common customs duties, and hence, there is no need for the costly and cumbersome rules of origin (RoO) requirements. Unlike Single Market, customs union does not entail free movement of people, being directly subject to European Court of Justice or contributing to the EU budget. However, a major problem with the new customs union is that, it will curtail UK's freedom to strike free trade deals for goods/commodities with other countries. On the other hand, if EU makes such deals with others, the UK market will be automatically open for duty-free import, without giving UK a reciprocal right. Nonetheless, UK may negotiate a comprehensive customs union, which at the same time, will give it the right to do trade deals and also have a say in any further EU free-trade negotiation. Considering all the options at hand, UK can opt to make the Norway-model as a first draft workable model, incorporating the closer-tied arrangement of customs union within its ambit. There are those, who feel that Norway-like arrangements will turn UK into a 'vassal state' which pays contributions to the EU, but has no say in the policymaking. But this line of argument does not hold sway if one delves deeper into the details of such arrangements.[6]

The type of trade deal UK will be able to strike in the end, will depend on EU's final stance in the upcoming negotiations, which will likely be tough. One reason the EU might take a hard stance is to transmit a strong message lest other member countries and Leave proponents are encouraged by the Brexit to follow suit. The initial reactions on the part of the European Commission was quite a

[3] Prime Minister May has rejected the Norway model (and the Canada-style, CETA arrangement) in hopes of a 'bespoke' trade arrangement, as said in her Brexit-related addresses.
[4] Corbyn in his Coventry speech on 26 February 2018 has remarked, that if elected, Labour government would go for a new comprehensive UK-EU Customs Union, but out of the Single Market. This was later backed by the Scottish Labour members.
[5] Monaco is a part of the EU customs territory through an agreement with France, and is administered as part of France. San Marino and Andorra are in a customs union with the bloc.
[6] The Norwegian contributions are mostly in the form of grants rather than payments to the central EU budget (for research or educational programmes like the Erasmus programme and for poorer countries) whose amount is controlled by Norway. Norway's trade with Europe is governed by the court of the EFTA whose rulings are advisory and lacks the power to fine member states that do not comply.

hardened one, which was conveyed by the EU President Donald Tusk's remarks, that there will be 'Hard Bexit or No Brexit' (Rankin and Stewart, 2016). After several rounds of discussion between the UK and EU negotiators, several informal meetings of the EU-27 member states, and a number of meetings between President Tusk and the UK Prime Minister Theresa May, significant progress has now been made in the Brexit negotiations (Annex Diagram 1). The European Commission has published a draft text of Brexit withdrawal treaty on 28 February 2018, which is basically the extension and presentation of the joint decisions taken by the UK-EU negotiating teams in legal terms (European Commission, 2018b). The EU perceives FTA as the only remaining possible model as voiced by President Tusk on 2 March 2018 while sharing the draft guidelines on framework for post-Brexit relationship between the EU and the UK (European Council, 2018).

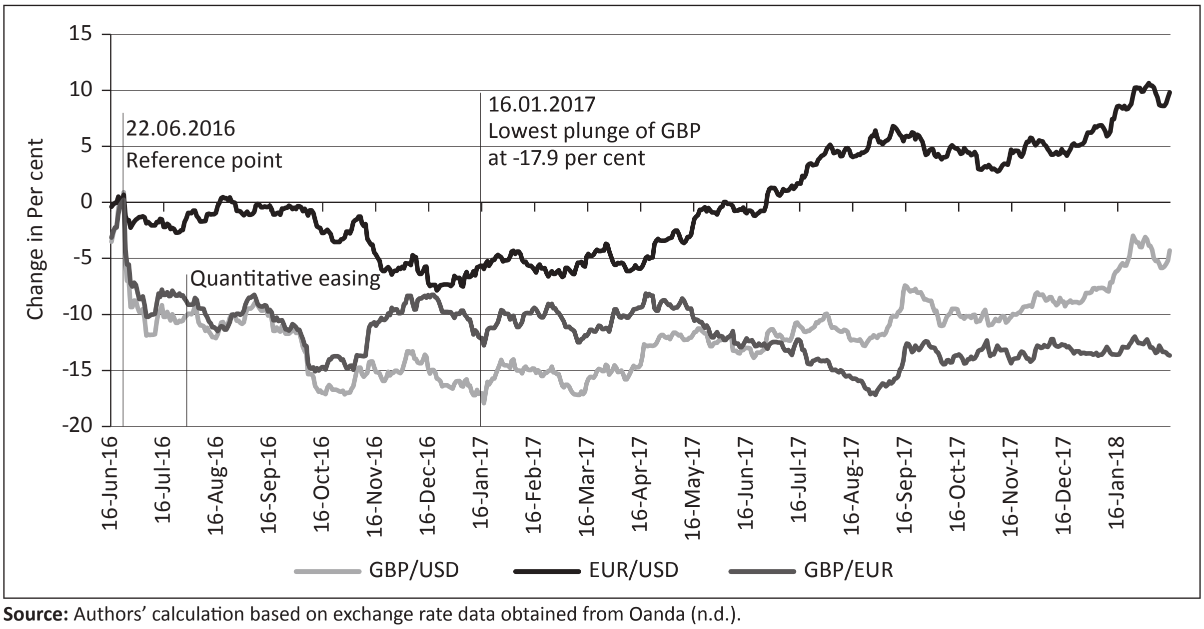
3. SHORT-TERM IMPACTS AND MEDIUM-TERM IMPLICATIONS OF BREXIT—A SURVEY OF LITERATURE

This section presents key findings of a review of some of the pertinent literature which have tried to capture the economic impact of Brexit from a range of perspectives—growth outlook, trade, investment, financial market, immigration and labour market, and political economy. While the possible implications can only be concretely estimated when the terms of Brexit will become clear, some analysts have tried to anticipate the impacts based on a number of assumptions, early signals transmitted by the market place, and based on the various likely scenarios.

According to several reputed institutions, such as the International Monetary Fund (IMF), World Bank, Capital Economics, Her Majesty's Government and Treasury, National Institute of Economic and Social Research (NIESR), Centre for Economic Performance of the London School of Economics, exit from the EU will be harmful to the interests of the UK economy. The impacts will be adverse in terms of economic growth, trade performance and investment flows. Stevens and Kennan (2016) forewarns, that adverse effects of Brexit could be significant for developing countries if appropriate remedial actions are not taken. On the other hand, some other studies, most notably by Economists supporting Brexit and Open Europe, based on a number of possible scenarios, found evidence of overall positive results.

The Brexit verdict has already left some visible footprints. This was manifested most prominently in the fluctuations of the exchange rate of British Pound (GBP) (fall in the value of the GBP) and volatility in

Figure 1: Change in GBP/USD, EUR/USD and GBP/EUR Rates with Respect to the Pre-Referendum Value



Source: Authors' calculation based on exchange rate data obtained from Oanda (n.d.).

the stock and bond markets. Annex 3 captures some of the immediate impacts of the EU-referendum result of Brexit as was experienced in foreign exchange and financial markets, perceptions and the immediate responses by the Bank of England. The GBP experienced a protracted period of volatility after the EU-referendum as can be seen in Figure 1. It plunged the lowest against the United States Dollar (USD) on 16 January 2017 amidst speculation about a 'Hard Brexit' in Prime Minister May's Brexit speech. The currency is yet to recover its pre-EU referendum value of USD 1.47 per GBP, and is still 4.29 per cent lower as of 14 February 2018. The fall was equally drastic against Euro (EUR), i.e. the GBP/EUR rate. One can find the same direction of movements in the EUR/USD, but to a lower extent. Euro seems to have recovered faster and to a greater extent with an interim deep plunge in the first-half of 2017. This can be attributed to strong economic tailwinds and phase-out of political uncertainties of several important elections in key EU economies.

3.1 Growth Outlook

Most of the research by the IMF, the Organisation for Economic Co-operation and Development (OECD), and NIESR was of the opinion, that the UK was likely to experience an economic slowdown following the Brexit, induced by uncertainties about the future, lower volume of trade, a loss of confidence in the financial market, weakened foreign investment prospects, and a possible shift of banks and financial hubs centering London, to elsewhere in the EU. Furthermore, restricted migration could lead to output losses with a detrimental effect on growth prospects. Growth forecasts made by selected organisations, based on research and survey (presented in the Annex Box 1), show the economic outlook to be a grim one. However, the growth of the UK economy in 2016 was 1.8 per cent and 1.7 per cent in 2017 (ONS, 2018a). There were no signs of recession in the post-referendum period, and consumer spending has remained fairly stable. The manufacturing sector of the UK has actually gained, thanks to the increase in competitiveness due to a weaker currency; resurgence in the global and the EU economy has also helped the UK. However, it is advisable to note that, the real impact for both UK and the EU is likely to be visible once the Brexit negotiations take a definite shape.

3.2 Trade Impacts

3.2.1 Trade Deal

A review of the relevant literature indicates that, Brexit will have a bearing on trade volumes, both to and from the UK. European businesses have invested heavily in the UK economy with supply and value chains involving the UK firms. These firms are likely to face significant impact, at varying ranges, depending on how the new UK-EU trade deal will shape up in the end. The upside for the UK economy is that, UK will be free to negotiate trade deals with other countries, according to UK's own domestic priorities; the downside of it is that, finalising trade deals is rather time-consuming, and the uncertainties resulting from the departure from current arrangements could undermine the interests of the UK firms and raise costs to the UK economy. Furthermore, UK will need to renegotiate trade agreements with more than 50 countries, with which EU currently maintains trade deals. Any trade deal with EU is likely to be less favourable for the UK than it is today, and UK firms will need to reposition in view of the emerging scenario. Similarly, EU will also face the consequences of changed perception when it will be making trade deals with a UK which is no more with the EU. When the UK renegotiates access to the Single Market, British firms will have to incur additional costs on account of customs clearance and administrative costs, and they may have to face non-tariff measures, such as quota and RoO requirements. This may result in some erosion of competitive strength of British firms. The EU consumers may suffer on account of higher prices of imports from the UK. Considering the above, it will be in the interest of both the UK and the EU to go for a deal that has a limited disruptive effect on the bilateral trade.[7] The dynamics of negotiation is likely to be more nuanced for trade in services since about half of the total trade is carried out with the EU (ONS, 2016).[8] Indeed, the Chequers proposal talks mostly about movement of goods, and not much about services and movement of people. As a briefing paper by the UK Trade Policy Observatory (Borchert and Tamberi, 2018) points out, value of services embedded in manufacturing exports of UK was equivalent to all direct financial and insurance services exported by the UK in 2017. Thus, the proposed changes in market access conditions was likely to have knock-on adverse effects on the demand for goods and services exported by the UK to the EU-27 countries.

3.2.2 UK Regaining WTO Status

One may expect complex negotiations as the UK accedes to the WTO after it exits from the EU (Ungphakorn, 2016; WTO Director-General Roberto Azevêdo in Miles, 2016); the same can be said of the EU. Both EU and the UK will have to renegotiate with all the WTO members to formulate and modify their separate WTO membership agreements. The EU is unique in having 29 members in the WTO (27 member states, the UK and the EU itself) with combined rights and obligations. The UK will have to revisit all current commitments of the EU in the WTO, and then determine its commitments in the WTO, following Brexit. Thus, any independent post-withdrawal trade arrangement for the UK will necessitate negotiations between the EU-27, the UK and other WTO members. The UK Government has to balance its trade policy considering the views of domestic stakeholders. For example, a policy of lower tariff and reduced agricultural subsidies is likely to be readily acceptable in the WTO, but would likely face significant domestic opposition in the UK. Similarly, trade in services is an area where the UK has strong interests. Accordingly, services negotiations, with the EU and in the WTO, will need to be carefully crafted if the UK is to maintain its current preeminent role. Also, any trade-related agreement must be consistent with the rules and provisions set out in the various WTO agreements (Soobramanien and Razzaque, 2016). WTO operates by consensus, not voting, and any country that perceives its interest to be affected by the independent trade policy of the UK, can disagree and open negotiations. UK can obviously decide to continue to follow a large part of the EU commitments—for example, bound tariff rates, market-opening pledges in the services sector, product standards and labelling, safety standards regarding food, among others. However, the WTO members will still need confirmation of the new provisions to be agreed through Brexit negotiations.

3.3 Investment

UK was the fourth largest destination in the world for foreign direct investment (FDI) inflow in 2015 (UNCTAD, 2016). Its preferential access to the EU market and the predominance of London as a global financial hub play important roles in this context. The attractiveness of the UK for investment may get undermined because of Brexit—it has lost four places in one year, and is now the seventh largest destination according to the World Investment Report 2017 (UNCTAD, 2017). Dhingra *et al*. (2016) had found by using statistical estimations (Bruno *et al*., 2016) that, EU membership increases FDI inflow by about 25 per cent (on an average) compared to what would be through FTA or MFN arrangements. Similar empirical evidence was also reported in Campos and Coricelli (2015) and Straathof *et al*. (2008). Any new arrangement with higher tariff and non-tariff barriers could make investment in the UK less attractive to potential investors. This likely fall in FDI is estimated to vary between 22 to 25 per cent, as per Dhingra *et al*. (2016) and Confederation of British Industry and PricewaterhouseCoopers (2016).

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[7]50 per cent of Britain's export is destined to the rest of the EU; in contrast, only 17 per cent of EU exports are meant for the UK. British export sector's dependence on the EU market is very high. At the same time, the UK is also an important market for the EU economies, when major economies of the EU are compared based on bilateral interdependencies with the UK (as revealed by the analysis of Capital Economics on percentage share of exports by destination in 2014, in Thomson Reuters Datastream) (Capital Economics, 2015).

[8]49.1 per cent of total exports are destined to the EU, and 53.4 per cent of total imports originate from the EU.

This lower inflow of FDI will have important adverse ramifications for the overall performance of the UK economy in the coming years.

3.4 Financial Market

London's current predominant role as the financial centre of Europe and the rest of the world, may come under question following Brexit. Companies which preferred London for its easy access to the EU market may think differently if 'passporting rights' are no longer available. The passporting rights allow countries (holding the rights) to sell authorised financial services to the EU market. EU rules and regulations may prove costly for an outsider and businesses may choose to move out of London to other competing financial hubs, such as Amsterdam, Dublin, Frankfurt and Paris. However, others feel that, London has already established a formidable competitive edge as a global financial hub. Replication of the London 'financial sector ecosystem' with its skilled workforce, legal framework, knowledge ecosystem and market infrastructure, is going to be costly and time-consuming (Global Counsel, 2015).

3.5 Immigration and Labour Market

Brexit will offer UK an opportunity to restructure its labour market and adopt new immigration policies. Control over immigration was one of the main motivations for the Leave campaign, which argued that, UK citizens were losing jobs to lower-waged/salaried migrants from the EU. UK has been focusing on curbing net migrant inflow, to 100 thousand annually, following the policy statement of the then Prime Minister Cameron. However, annual migration to the UK has been increasing over the past years with net inflow to the tune of 333 thousand in 2015 (Barett, 2015). UK's net migration was at its peak of 336 thousand in June 2016 (month of EU-referendum); for the following one year, it had come down to 230 thousand. The Office for National Statistics (ONS) data shows that, the fall was primarily on account of EU citizens who were leaving. Indeed, net EU migration to the UK peaked till the referendum year and has now halved. Prime Minister Theresa May stands firm on this target (100 thousand); there has also been mention of curbing immigration in the White Paper. This will mean a significant loss in remittances for many countries. It should be noted that, reduced migration could lead to higher production costs and the loss of competitiveness of tradable sectors in the EU. Much will also depend on whether the UK chooses to replace relatively high-cost EU migrant workers by those from non-EU (Asian and African) countries by taking advantage of the newly gained labour market flexibility. Wadsworth *et al*. (2016) has shown that, there is no significant evidence of immigration harming the UK economy. Rather, it is observed that, immigrants benefit the UK economy by offering a wide pool of skills and contributing to the exchequer. When a wide range of skills are incorporated in the national economy, it leads to increased productivity, which in turn, increases the average wage.

It has been widely argued that, withdrawing from the EU was likely to lead to job losses and a rise in unemployment in the UK. According to forecasts by the Bank of England, job losses could be to the tune of 250 thousand with an expected rise in unemployment from 4.9 per cent in March–May 2016 to 5.4 per cent in 2017, and 5.6 per cent in 2018 (Kollewe, 2016). However, unemployment is at the lowest level of 4.2 per cent for March–May 2018 period since 1975 (ONS, 2018b).

3.6 Political Economy

Post-Brexit political dynamics will likely shift significantly, within the EU and the UK. The political contagion of the 'exit sentiment' is an emergent worry. Recent elections in France, Germany, Italy and Netherlands have witnessed strong 'Eurosceptic' voices in the election campaigns, arguing in favour of 'negotiating the terms of the EU membership' at best, and various nomenclatures of 'exit' at the worst.

In the UK itself, Scotland and Wales, which had the majority voters favouring Remain, have threatened to go their own ways if needed.[9]

It also needs to be kept in mind that, the UK holds significant soft and hard power. UK ranked third in the Monocle Soft Power Index 2015[10], and seventh in military spending, which was USD 54.2 billion in 2016 (SIPRI, 2016).[11] Thus, without the presence of the UK, EU will lose its weight as a bloc in the global interplay of power politics. Its voice in fora such as the Group of Eight (G8), Group of Twenty (G20), IMF and the World Bank will be weakened.

All the above will have important implications for UK's partner economies as well. There are a number of transmission channels through which this could happen including market access, trade, remittance, investment and official development assistance (ODA).

4. LIKELY IMPACT OF BREXIT FOR BANGLADESH

UK is a major economic partner of Bangladesh, with the bilateral relationship spanning a wide range of areas including trade and commerce, business, source of FDI and remittances, aid and development support, and people-to-people contact. Table 1 presents some relevant information in this connection. State visits by the UK Government officials have consistently reassured Bangladesh of this support to this bilateral relationship. This assurance may only be materialised if Bangladesh is prepared to hold effective negotiations to address the details of the new arrangements in the bilateral relationship as a graduating LDC, or as a part of the Commonwealth cohort. Taking cue from the above, the following section delves deep into the most important aspects of the Bangladesh economy which will experience the impact of Brexit.

Table 1: Economic Importance of the UK for Bangladesh[12]

Bangladesh-UK Relationship Dynamics	**FY2015**	**FY2016**	**FY2017**	**FY2018**
Exports to the UK (billion USD)	3.20	3.80	3.60	4.00
Exports to the UK as % of total global exports	10.90	10.60	9.90	10.90
Exports to the UK as % of total EU exports	20.20	19.00	19.00	18.70
Exports to the EU as % of total exports	53.80	55.90	52.00	58.20
Imports from the UK (billion USD)	0.32	0.27	0.33	-
Imports from the UK as % of total imports	0.80	0.70	0.80	-
Remittance received from the UK (billion USD)	0.80	0.90	0.80	1.10
Remittance as % of total from the world	5.30	5.78	6.30	7.40
Stock of FDI received from the UK (billion USD)	1.40	1.50	1.60	-
as % of total FDI stock	10.90	10.40	11.20	-

Source: Authors' compilation from EPB (2018); Bangladesh Bank (n.d.).

[9]As reported in the Guardian (Carrell and Brooks, 2016), the first minister of Scotland, Nicola Sturgeon has expressed preparedness for another independence referendum if deprived of full access to the Single Market after Brexit. The Scottish Independence Referendum was held on 18 September 2014, to decide on the country's independence. The 'No' side won by 55.3 per cent to 44.7 per cent of 'Yes', to the referendum question 'Should Scotland be an independent country' (GOV.UK,n.d.b).

[10]The index is prepared by the Monocle Soft Power Survey (2015). Soft power is defined as the power to modify (or manipulate) another country's behaviour by means of appeal and persuasion, rather than coercion, which stands for hard power, as demonstrated by financial, foreign policy and military strengths. The primary determinants of soft power are culture, political values and diplomacy. The UK flexes significant soft power.

[11]Countries above UK are: USA (USD 606 billion); China (estimated USD 226 billion); Russia (USD 70 billion); Saudi Arabia (USD 61 billion); and France and India (both USD 56 billion).

[12]Some of the other important dynamics of UK-Bangladesh bilateral relationship are: (a) Bangladesh is the seventh most common country of birth and nationality in the UK—2.8 per cent of the foreign-born in the UK originate from Bangladesh; (b) Bangladesh is the country of birth for 4.6 per cent of all foreign-born persons living in London—ranking third in the list to India (8.9 per cent) and Poland (5 per cent) (The Migration Observatory, 2018); (c) The cumulative UK aid received by Bangladesh since its independence till FY2016-17 is USD 2.7 billion (ERD, n.d. [Table 5.0]).

4.1 Trade Performance

The UK is a major player in the export scene of Bangladesh—the third single largest export destination after the United States of America (USA) and Germany. UK accounted for 10.9 per cent of Bangladesh's total global exports; 18.7 per cent of exports destined for the EU market in FY2017-18. Out of USD 3.81 billion worth of exports to the UK in FY2017-18, USD 3.53 billion was contributed by the export of readymade garments (RMG) goods (92.5 per cent). Besides textiles and apparels, the footwear sector has also been experiencing high growth in the UK in recent years.[13] Other important exports to the UK have been frozen foods, light engineering products, etc.

Bangladesh exports to the EU enjoy duty-free quota-free (DF-QF) market access for all exports but arms[14], under the EU's generous Generalised Scheme of Preferences (GSP) offer for the LDCs.[15] An analysis of the product-wise export receipts (at 6 digit Harmonised System (HS) code level) for FY2017-18 from the UK was carried out to identify top 20 exports, which accounted for 76.5 per cent of total export receipts from the UK (EPB, 2018).[16] It is estimated that, for importing these items, UK importers would have to pay USD 366.2 million as duties, had there not been any preferential market access under the EBA, that is, if exports had to face MFN tariffs in the UK (at EU-side common customs area duties).[17] Since the overwhelming part of Bangladesh's export to the UK is consumer items, demand of which tends to be price elastic, duty-free access has considerable positive effect on both demand and competitive strength of the Bangladeshi exports to the UK. Besides, many EU importers tend to import through the UK for onward shipment to the other EU countries, taking advantage of the EU-wide free trade area (duty-free market access under the EU Customs Union). These exports are also likely to be affected, in varying degrees, depending on the terms of Brexit to be negotiated in the coming days.

Exports from Bangladesh are produced and marketed according to the product standards and certification procedures applicable under the current trading arrangements with the EU. If more stringent standards are imposed by UK after the separation, for example with regard to Intellectual Property Rights (IPR) or Sanitary and Phytosanitary (SPS) measures applicable under the trading specifications of the UK, this may negatively affect Bangladesh's exports to the UK.

Exports to the UK will also depend on how the post-Brexit UK economy fares in terms of its likely impact on consumer behaviour, and consumer confidence and overall gross domestic product (GDP) growth. With regard to market access conditions, several scenarios may be envisaged—ranging from maintaining an EBA-type scheme for the LDCs to applying the MFN rates, and something in between. A study by Stevens and Kennan (2016) cautions that, if the UK adopts the MFN regime similar to that of the EU Customs Union, Bangladesh will be the country which will be the hardest hit among all the countries which receive 'better-than-MFN' market access facilities from the EU.[18] The likely additional import duty payment by UK importers is estimated to be equivalent to 11.7 per cent of UK's total

[13]During FY2011-12 to FY2015-16, the footwear export experienced an annual average growth of 27.5 per cent.

[14]All 7,220 tariff lines from the LDCs are duty-free, except arms and armaments, which falls under the HS Code Chapter 93.

[15]The GSP for the developing countries and the LDCs was first adopted in 1968, and became effective in 1971. EU GSP offers market access at either lower tariffs, or fully duty-free access for imports from 90 developing countries and territories into the EU market. The EU GSP is provided with the objective of stimulating economic growth, job creation and sustainable development through higher exports from beneficiary countries (EPB, n.d.; European Commission, n.d.c).

[16]Top 20 products have an export earnings of USD 3.05 billion, and includes RMG manufactures mostly (19 items), and frozen food (EPB, 2018).

[17]Calculation made by authors, using data of export receipts from EPB (2018) and MFN tariff data from European Commission (n.d.b).

[18]UK importers importing from Bangladesh will have to pay duties worth EUR 247 million (USD 305.9 million) at the prevailing MFN rates. In Stevens and Kennan (2016), the calculation of potential calculable tax hike is done based only on highest applicable ad valorem element (8 digit trade code) with data collected from the EU's 2015 schedules in the TRAINS database of the United Nations Conference on Trade and Development (UNCTAD). The average annual imports in 2013–2015 from the Commonwealth countries were used for this analysis. Exchange rate used was of 14 February 2017, where 1 EUR = 1.24 USD (Oanda, n.d.).

import payments in case of Bangladesh.[19] If the UK does not offer any preferential market access to the LDCs, and in case LDCs such as Bangladesh have to face MFN duties, there is likely to be serious loss of export competitiveness for these LDCs.

In their joint statement made on 25 June 2017, Liam Fox, MP, Secretary of State for International Trade and Priti Patel, former MP and Secretary of State for International Development had assured Bangladesh and other beneficiaries of the EU's EBA, that the UK will continue to provide preferential market access to these countries following the Brexit (Department for International Development and Department for International Trade, Government of UK, 2017). This is a welcome and reassuring commitment which has been appreciated by all. However, trade deals are never simple and the devil lies in the details. In case of an FTA between the UK and the EU, RoO will be a key consideration. As was pointed out in a post published by the UK Trade Policy Observatory, setting the RoO and putting in place the procedures and enforcement mechanisms will entail extra time, effort and costs for UK exporters (Winters and Tamberi, 2018). This argument can be extended also in case of Bangladesh-UK trade. Even if UK agrees to continue to extend duty-free market access for products of exports originating from the LDCs such as Bangladesh, the RoO will need to be fixed anew. If these are different from those currently in place under the EBA, Bangladesh will need to set up new procedures, regulations and enforcement modalities to ensure compliance with the changed RoOs, not to speak of ensuring capacity towards RoO compliance. New supply-side capacities may also need to be built to ensure compliance with the new RoOs. Bangladesh should be prepared for negotiations with the UK, so that terms for preferential market access remain unchanged (does not become more stringent); this is particularly relevant for the RoO.

Initial post-referendum appreciation of Bangladeshi Taka (BDT) against the GBP (as seen in Figure 2) made Bangladeshi products more expensive for UK importers. The consequent 'price effect' had negative implications for Bangladesh's export to the UK market. Though Bangladeshi goods do not face competition from UK's domestically produced goods, the appreciation of BDT compared to other competitor countries' currencies (Table 2) had affected the competitiveness of Bangladeshi exports in the UK market. The analysis presented in Box 2 shows that, the response in the currency market was not just a knee-jerk reaction; there are deeper anxieties embedded in the market behaviour. The value of GBP is rather volatile at present; GBP will tend to plunge deep or rise up—depending on the state of UK-EU negotiations (Figure 2). This volatility does not fare well for exports of Bangladesh to the UK, since most of the Bangladeshi exports to the UK are highly price-sensitive—hence, the apprehension about loss in export earnings.[20] This was reflected in the 7.1 per cent fall in exports in July 2016, immediately following the EU-referendum. Indeed, exports to the UK faced negative growth all through FY2016-17 when compared to FY2015-16. On the other hand, imports from the UK[21] will be cheaper for Bangladeshi importers if BDT appreciates. This will make imports from the UK a relatively more lucrative business proposition. Consumers and importers of intermediate inputs from the UK will stand to benefit from this.

Export data for the post-referendum period shows that, exports to the UK fell by 6.3 per cent in FY2016-17. However, this has recovered later. Export for the first six months of FY2017-18 rose by 19 per cent over the corresponding period of FY2016-17. This direction was true for RMG exports—July–

[19]Bangladesh comes third relative to Seychelles (23.4 per cent) and Malta (14.3 per cent). The extra import duty payment amounts to 1.7, 9.2 and 2.3 per cent of their respective exports to the UK for other Asian Commonwealth members, i.e. India, Pakistan and Sri Lanka (Stevens and Kennan, 2016).

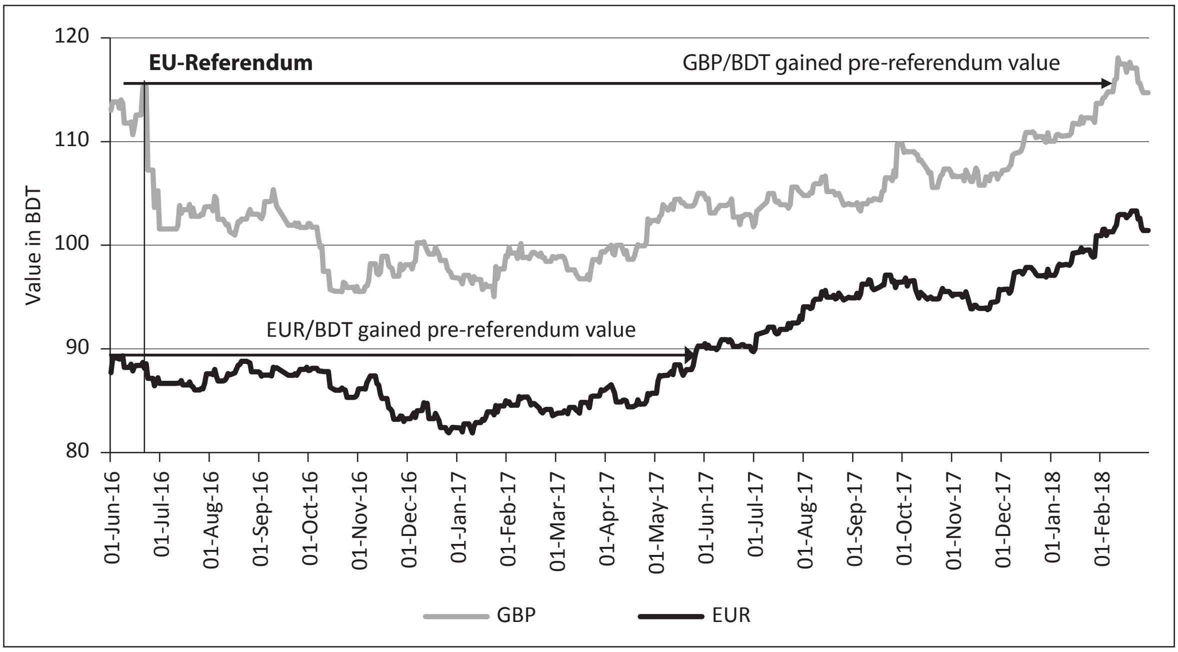
[20]According to a briefing paper of the Overseas Development Institute (ODI) (Mendez-Parra *et al.*, 2016), Bangladesh's exports to the UK could fall by 1.2 per cent as a result of the appreciation of BDT (weaker—a 10 per cent depreciation). Expected export downfall is 0.9 per cent for Cambodia, 0.4 per cent for India and 0.6 per cent for LDCs (estimate based on the assumption of unit elasticity). The ODI study projects that, Bangladesh will experience a fall in exports equivalent to USD 299.8 million.

[21]Bangladesh made 0.8 per cent of its non-EPZ import payments to the UK in FY2014-15 (Bangladesh Bank, n.d.).

Box 2: Post-EU-Referendum Exchange Rate Movements

GBP in terms of BDT fell from 115.3 to 107.3 on the Brexit referendum day (Thursday, 23 June 2016), and plunged deeper to BDT 103.6 on 27 June 2016, as shown in Figure 2. With some volatility, this trend had continued over the next few weeks following the referendum. The lowest exchange rate was experienced on 16 January 2017, when GBP's value came down to BDT 95. The pre-referendum level was regained at the end of January 2018—this was contributed largely by the continued depreciation experienced by USD/BDT since November 2016.[22] Since USD/GBP has still not recovered, one cannot rule out the volatility induced by the uncertainties of the upcoming negotiations and post-Brexit scenario. On the other hand, BDT's value against EUR reverted back to pre-referendum level (1 EUR = BDT 88.6) on 14 August 2016, which was followed by a fall, and finally rise to pre-referendum value on 11 May 2017. It is to be noted that, EUR/BDT rates recovered faster than GBP/BDT rates.

Figure 2: BDT per GBP and EUR



Source: Authors' calculation based on exchange rate data obtained from Bangladesh Bank (n.d.).

Table 2 shows the appreciation of BDT along with some of its competitor countries' national currencies. It is interesting to note that, only BDT appreciated by 1.5 per cent on the day of the EU-referendum, while Indian Rupee (INR) and Chinese Yuan (CNY) experienced depreciation, and Vietnamese Dong (VND) remained unchanged. On the other hand, immediately after the referendum (on 24 June 2016), VND appreciated the highest. It is seen that, INR experienced the highest appreciation (25 per cent), followed by BDT (23.6 per cent), and CNY experienced the lowest (18 per cent) appreciation against the GBP. BDT's highest appreciation was to the tune of 9.7 per cent against EUR; in case of India, this was 12.2 per cent.

Table 2: Appreciation of Currencies of Bangladesh, China, India and Vietnam

(in Per cent)

Time	BDT	CNY	INR	VND
Day of EU-referendum: 23 June 2016[a]	1.5	(-) 0.8	(-) 0.6	0.0
Comparing values on the day immediately after EU-referendum (24 June 2016)[a]	6.0	5.1	5.2	6.7
Comparing average values for the week prior to and following EU-referendum[b]	7.0	6.0	5.9	6.5
Comparing average values for the month prior to and following EU-referendum[c]	7.6	6.1	9.1	9.1

(Table 2 contd.)

(Box 2 contd.)

[22]USD/BDT depreciation in 2017 was 5.08 per cent.

(Box 2 contd.)

(Table 2 contd.)

Time	BDT	CNY	INR	VND
On 24 October 2016[a]	20.9	17.0	21.6	20.0
On 31 March 2017[a]	15.7	12.4	22.8	16.7
On 14 February 2018	2.4	11.4	9.6	6.7
Highest appreciation against GBP[a]	23.6	18.0	25.0	23.3
Highest appreciation against EUR[d]	9.7	2.9	12.2	7.7

Source: Authors' calculation based on exchange rate data obtained from Oanda (n.d.).

Note: [a] The value on this date has been compared to that of the day immediately before the referendum, 22 June 2016.

[b] The week prior to EU-referendum is from 16 to 22 June 2016, and the week post-EU-referendum is from 24 to 30 June 2016. The averages for these two weeks were calculated, and then compared to check the week-wise appreciation of the local currencies.

[c] The month prior to EU-referendum is from 22 May to 22 June 2016, and the month post-EU-referendum is from 24 June to 24 July 2016. The calculation process was similar to Note 'b' above.

[d] Only calculation for EUR, all other calculations are for GBP.

December FY2017-18 earnings are 20.7 per cent higher than that was for the same period in FY2016-17 (EPB, 2018). The initial shock of EU-referendum result and subsequent GBP depreciation appears to be over by now. On the other hand, Bangladesh will need to be watchful of how the scenario unfurls during the run-up to 2019, or till the time when the transition period ends.

From the above discussion on the dynamics of Bangladesh's trade with the UK, it is evident that, exports of Bangladesh to the UK are relatively more susceptible to adverse effects induced by the Brexit; in case of imports from the UK, the effects are relatively muted. In this connection, an econometric analysis using an augmented gravity model has been carried out to understand the ramifications of Brexit on exports from Bangladesh.

4.1.1 An Econometric Analysis of the Implications of BREXIT on Bangladesh's Exports[23]

The underlying equations for the gravity model regressions are as follows:

$$\begin{aligned}\ln(export\ volume_{ij,t}) &= \alpha_{ij} + \beta_1 \ln(GDP_{\ j,t}) + \beta_2 \ln(GDP_{\ i,t}) + \beta_3 \ln(population_{\ i,t}) \\ &+ \beta_4 \ln(population_{\ j,t}) + \beta_5 \ln(distance_{\ ij}) + \beta_6 \ln(tariff_{\ j,t}) \\ &+ \beta_7\, eu_{dummy_{if\ EU=1}} + \beta_8 \ln\left(RERE_{i/_{j},t}\right) + \mathrm{u}_{ij,t}\end{aligned} \qquad \text{(i)}$$

$$\begin{aligned}\ln(export\ volume_{ij,t}) &= \alpha_{ij} + \beta_1 \ln(GDPPC_{\ j,t}) + \beta_2 \ln(GDPPC_{\ i,t}) + \beta_5 \ln\ (contiguity_{\ ij}) \\ &+ \beta_5 \ln(distance_{\ ij}) + \beta_6 \ln(tariff_{\ j,t}) + \beta_7\, eu_{dummy_{if\ EU=1}} + \beta_8 \ln\left(RERE_{i/_{j},t}\right) \\ &+ \mathrm{u}_{ij,t}\end{aligned} \qquad \text{(ii)}$$

$$\begin{aligned}\ln(export\ volume_{ij,t}) &= \alpha_{ij} + \beta_1 \ln(GDPPC_{\ j,t}) + \beta_2 \ln(GDPPC_{\ i,t}) + \beta_5 \ln\ (contiguity_{\ ij}) \\ &+ \beta_5 \ln(distance_{\ ij}) + \beta_6 \ln(tariff_{\ j,t}) + \beta_6 \ln(tcost_{\ ij,t}) + \beta_7\, eu_{dummy_{if\ EU=1}} \\ &+ \beta_8 \ln\left(RERE_{i/_{j},t}\right) + \mathrm{u}_{ij,t}\end{aligned} \qquad \text{(iii)}$$

[23] The technicalities of this econometric analysis has been presented in detail in Annex 4.

In the above equations, *i* and *j* denote Bangladesh and the importing country respectively, and *t* denotes time. Here, α_{ij} stands for the individual country pair (origin-destination) effects, and $u_{ij,t}$ is the error term. Equation (i) is the basic augmented gravity model equation with the variables as discussed before.[24] Equations (ii) and (iii) consider the per capita incomes for both trading countries instead of considering income and population separately. Equation (iii) includes the variable $tcost_{ij,t}$, which is the ad valorem trade cost between countries *i* and *j*.

Results of the analysis are presented in Table 3. It is revealed that, the income of the importing country has a positive and significant impact on the exports of Bangladesh on an average; a more developed economy with a higher GDP tends to import more due to high aggregate demand (Columns A and B); higher GDP per capita indicates more purchasing power, and hence, higher demand for imported goods (Columns C-E). This implies that, if after Brexit, the UK economy has sluggish GDP growth or consumer confidence suffers, the growth of exports from Bangladesh to UK is likely to fall. In standard gravity models, distance is considered as a logical proxy for trade costs in terms of transportation costs. Analogous to literature-based expectations, one finds an increase in distance to have a negative and significant[25] impact on the exports of Bangladesh. However, this is not completely applicable in case of Bangladesh. An examination of export trends of Bangladesh indicates that, most of its exports are destined to non-contiguous[26], distant countries such as the USA, Canada, EU member countries; this may partly be on account of preferential market access in these markets. But distance may prove to be a significant constraining factor in trading with UK, if the generous GSP scheme currently in place is no longer applicable.

The estimated coefficient of the variable real exchange rate $(RERE_{i/j,t})$ is significant and positive in all the regressions. Column (A) shows that 1 per cent increase in real exchange rate (because of depreciation of BDT or appreciation of the importing country's local currency unit) will, on an average, cause an increase of 0.28 per cent in the export value of Bangladesh to that country (*ceteris paribus*). The result strongly indicates a reduction in exports to the UK as a result of the recent significant fall in the value of GBP and the consequent appreciation of the BDT.

Tariff $(tariff_{\ j,t})$ is a continuous trade policy variable, and is supposed to have a significant and negative impact on the value of exports. However, in the current analysis, only Poisson Pseudo Maximum Likelihood (PPML) estimation of equation (i) (Column B) suggests the presence of adverse effects of tariff on Bangladesh's exports.[27] It may thus be concluded that, if Bangladesh does not negotiate favourable and 'better-than-MFN' tariff rates after the UK leaves the EU, exports to UK could suffer a significant decline.

The negative and significant coefficient estimate of the trade policy variable—ad valorem trade cost $(tcost_{\ ij,t})$, suggests that, a 1 per cent increase in trade cost would lead to a decrease of exports for Bangladesh to the tune of 3.1 per cent (Column E). Thus, if the new UK-Bangladesh trade arrangement has more stringent regulations and higher tariff rates leading to a 1 per cent increase in trade cost, then this would mean a loss of USD 122 million, considering the export figure to the UK for FY2017-

[24]In equation (i), the usual gravity dummy variables used to describe country pair effect characteristics, such as common language, distance and contiguous border, were initially considered. However, variables common language and common coloniser got omitted from the regression because of collinearity. The model was subsequently rerun without these variables.

[25]The coefficient of the variable 'distance' is significant in all results, except in Column E where 'trade cost' is actually considered.

[26]This also explains the inconsistency observed in the estimates obtained for the variable 'contiguity of borders'.

[27]One viable explanation, as per Cipollina and Salvatici (2013), is that using aggregated trade flows (as has been used in the current analysis) to analyse the impacts of trade policy measures such as tariff, which are applied at disaggregated levels (at product levels), can give misleading results. They showed in their work, that the coefficient of tariff variable gets significant, once product level disaggregation (at HS 6 digit level) is considered. It suggests that product-level disaggregated data can better capture the supply capacity, utilisation of preferential market and sectoral erosion.

18.[28] The loss can increase if we consider the fact that the UK acts as the hub for import of Bangladeshi goods to other EU countries; any unfavourable change in UK-Bangladesh trade relations will affect exports to these EU countries as well.

The coefficient of the EU dummy variable $eu_{dummy_{if\ EU=1}}$ is statistically significant for all the equations, under all estimation techniques. This implies that, EU membership of the importing country

Table 3: Regression Results for the Gravity Model

Explanatory Variable	Dependent Variable: Log of export value in USD				
	Equation (i)		*Equation (ii)*		*Equation (iii)*
	LSDV Fixed Effect Model (A)	PPML Estimation (B)	LSDV Fixed Effect Model (C)	PPML Estimation (D)	LSDV Fixed Effect Model (E)
Log of GDP of importing country	0.42 (1.92)	0.05 (11.01)**	-	-	-
Log of GDP of Bangladesh	1.34 (5.66)**	0.07 (5.26)**	-	-	-
Log of per capita GDP of importing country	-	-	0.67 (5.45)**	0.01 (2.33)*	0.63 (3.28)**
Log of per capita GDP of Bangladesh	-	-	1.50 (8.16)**	0.10 (15.54)**	-
Log of population of Bangladesh	-	-0.11 (1.58)	-	-	-
Log of population of importing country	-0.59 (1.21)	0.01 (2.20)*	-	-	-
Contiguity of borders	-	-	-1.20 (2.23)*	0.01 (0.57)	2.14 (6.10)**
Log of distance between Dhaka and respective capitals of importing countries	-1.36 (2.24)*	-0.05 (9.55)**	-1.16 (5.09)**	-0.01 (2.51)*	-0.04 (0.23)
Log of tariff rates	0.09 (0.66)	-0.01 (2.25)*	-0.002 (0.02)	0.003 (0.57)	0.01 (0.13)
Log of ad valorem trade cost	-	-	-	-	-3.07 (10.45)**
EU dummy	0.43 (2.06)*	0.05 (10.79)**	0.71 (5.09)**	0.04 (7.39)**	0.48 (1.98)*
Log of real exchange rate	0.28 (9.01)**	0.01 (9.17)**	0.18 (8.74)**	0.02 (19.95)**	0.09 (3.35)**
Constant	-5.97 (0.52)	2.22 (2.22)*	11.69 (5.08)**	2.32 (37.20)**	27.35 (16.33)**
N	621	621	1113	1113	745
R^2	0.88	0.79	0.90	0.57	0.90
Adjusted R^2	0.87	-	0.89	-	-
F-test	66.50**	-	103.12**	-	-
Pseudo log-likelihood	-	-1480.50	-	-2690.64	

Note: 1. LSDV (model): Least Square Dummy Variable.
2. * and ** denote that the coeffecients are significant at 95 per cent and 99 per cent confidence intervals respectively.
3. Time and country-pair effect dummies for LSDV model are not included.

[28] The loss would be USD 111 million for FY2016-17 export earnings figure, and USD 118 million for that of FY2015-16.

has a significant and positive effect on the exports of Bangladesh. From a reverse point of view, this would indicate the possible negative effect of termination of EU membership of an importing country. It is obtained from further calculations[29] that, Bangladesh could lose approximately USD 300 million of export earnings (7.5 per cent of FY2017-18 export earnings from the UK) to the UK as a consequence of the Brexit, if an appropriate compensatory preferential market access mechanism is not put in place. This emphasises the importance of negotiating a suitable trade deal with the UK in view of the Brexit.

4.2 Migration

As some of the information provided in Table 1 highlights, UK has been an important destination for migration of Bangladeshis. Through a steady influx of migrants over the past many years, there is now a large Bangladeshi community living in the UK. There is a wide recognition that this diaspora has contributed significantly to the British society and economy. Migration was an important issue in the discussion and debate which preceded Brexit referendum. Perceived adverse impact of migration—job loss, pressure on housing and rent, access to health and other services—was a key argument put forward by the Leave campaign.

As part of the policy of reducing the number of immigrants, while complying with the EU policy of free movement, the UK had imposed a bar on non-EU immigrants. Stringent visa requirements and binding employment rules have made it very difficult for Bangladeshi (along with Indian and Pakistani) businesses to hire people with the right skills from South Asia. Since the UK Government had no power to exercise in containing the inflow of migrants from the EU countries, it was mainly the non-EU migrants who were affected by the policy of curbing migration. For example, the curry business owned mostly by Bangladeshis was hit hard, and businesses were closing at the rate of at least two-five per week due to a shortage of skilled chefs.[30] The Bangladesh Caterers Association (BCA) and other business communities who relied on specific skills, are hoping to take advantage of the emerging situation in the UK, as it will no longer be bound by the EU policy of free access of labour. Brexit brought hopes of fair competition between EU and non-EU migrants in terms of getting access to the UK economy based on skills. The 4-billion-pound curry industry backed Brexit in this hope, and also under the persuasion of several pro-Brexit parliamentarians, who vouched to push for a point-based immigration system[31], which can bring in people with the right set of skills. They advocated that, once out of the EU, the UK will not have to reduce non-EU migration explicitly to curb net inflow. However, Prime Minister May has already revoked the idea of having a point-based system for immigration under the claim that it does not allow much control to the government, and thus, fails to address the purpose of Brexit. In a statement published on 6 September 2016, the UK Government came up with the proposal to devise an immigration system that gives it more control than the point-based system (Department for Exiting the European Union, 2016). However, no details have been sketched out as yet. If the UK is to remain competitive in the global market, it will need low-waged labour which Bangladesh and other South Asian countries are in a position to supply. But this will call for taking adequate preparation in terms of enhancing skills which match the required set.

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[29] Authors' calculation based on the coefficient obtained and data on exports for FY2015-16.

$$loss\ in\ exports = \frac{\Sigma_{EU(selected\ 19)}\, exports}{\Sigma_{EU(28)}\, exports} * \left(\left(e^{\beta_{EU\ dummy}} - 1\right) * 100\right)\% * \frac{total\ exports\ to\ the\ UK}{\Sigma_{EU\ (selected\ 19)}\, exports} * exports_{UK}$$

[30] Taking the curry industry as an example, one observes how Bangladeshi businesses were hurt due to stringent migration policies. Restaurants were shutting down due to lack of skilled chefs (as was stated by the President of BCA, Pasha Khandakar). Moreover the UK law of pinning wage significantly (GBP 5,000) higher than the current market average had adversely impacted on the bottom line, and reduced the profit margins of enterprises. Additionally, the idea of employing and training British, Czech and Polish people for these jobs did not help either. This problem in the curry industry shows the deep anxieties caused by stringent migration laws and binding laws on employment of immigrants (The Telegraph, 2015).

[31] The Australia-style point-based immigration system grants immigration if the applicant meets a set of criteria set by the host country authority.

4.3 Remittance

Remittance flow plays an important role in the Bangladesh economy—at the macro-level it is a major source of foreign exchange which supports the balance of payments of the country. At the micro-level, remittance tends to be the principal source of household income, which supports basic consumption, investment in healthcare and education, and even entrepreneurship. In 2016, remittance received by Bangladesh was equivalent to about 6.1 per cent of its GDP (it was as high as 10.6 and 9.2 per cent in 2012 and 2013) (Bangladesh Bank, n.d.). Barring the recent volatility (fall) in the flow, remittance has traditionally provided Bangladesh with a stable flow of private capital (World Bank, 2015).

It is a fact that the UK has been a major source of remittance—Bangladesh is in the top-10 key receivers of remittance from the UK. In FY2016-17, Bangladesh received 6.3 per cent of global remittance flows from the UK, and 7.4 per cent in FY2017-18 (Table 1). Remittance flow did experience shock emanating from Brexit referendum as reflected by the negative month-on-month growth for July 2016 ((-) 52 per cent); in fact, it was negative through the first half of FY2016-17. This sharp fall has most likely been caused by the devaluation of the GBP. In the face of this, there are several possibilities: a large part of remittance may have been diverted to informal channels or remitters may have held back in hopes of currency markets gaining stability. For instance, an individual remitting GBP 100 to Bangladesh in July 2016 would be able to send USD 142 (i.e. BDT 11,140) if per pre-referendum rates prevailed; but after the fall in the value of GBP, the same amount was equivalent to USD 131.4 (i.e. BDT 10,303) only, thus making a loss of BDT 837.[32] This loss is significant if at micro-level monthly household income is considered. Remittance flow in total has increased following the EU-referendum as the GBP/BDT rates improved, and also thanks to the depreciation of USD/BDT rate in 2017, in the 'managed' floating exchange rate regime of Bangladesh (Figure 2). Future remittance flow from the UK will depend on the migration policy pursued by post-Brexit governments. Some quarters among the Bangladeshi migrants in the UK hope that the post-Brexit UK will try to replace high-waged East-European workers by relatively low-waged workers from countries such as Bangladesh. It is, however, too early to test this hypothesis.

4.4 Foreign Direct Investment

UK's overseas investment is significant. Indeed, UK is a major foreign investor in Bangladesh. According to Bangladesh Bank (n.d.) data, UK was the second largest investor in Bangladesh in FY2016-17, with FDI stock of USD 1.6 billion (Table 1). The major share of this was in Banking (53.9 per cent), textile and apparels (15.9 per cent), and food industry (11.5 per cent). At present, over 240 UK companies have some type of investment in Bangladesh. The fall in the value of GBP could adversely affect UK investment in Bangladesh, as it will make local procurement in the country costly in GBP terms. On the other hand, earnings in Bangladesh will bring higher income when transferred to GBP. Thus, the overall impact remains somewhat uncertain. Though net FDI inflow from the UK had shown a lower growth after the referendum, much will depend on the impact of Brexit on UK's economic performance and outlook in the medium term.[33] UK Government officials visiting Bangladesh have expressed keen interest in increasing investment in Bangladesh[34], this opportunity can only be materialised with proper preparation. Developed infrastructure, easy access to energy, trade facilitation and speedy establishment of the special economic zones (SEZs) will play important roles in this regard.

[32]For this calculation, monthly average exchange rates have been used from the Bank of England (GBP/USD 1.42 for June 2017 and 1.31 for July 2017), and the Bangladesh Bank (USD/BDT 78.4), as accessed in March 2018.

[33]Net FDI inflow from the UK for the period of January–June was USD 154.7 million for 2015, USD 160.8 million for 2016 (increased by 4 per cent), and USD 144.4 million for 2017 (decreased by 10 per cent compared to 2016). FDI stock from the UK registered a growth of 17.9 per cent in FY2015-16.

[34]Notably by UK's trade envoy for Bangladesh, Rushanara Ali, upon her visit to Bangladesh in December 2016.

4.5 Foreign Aid

According to FY2016-17 data, UK is the sixth largest source of financial assistance to Bangladesh. Bangladesh was UK's ninth largest ODA recipient in 2016; 14.9 per cent of the ODA the country received, was from the UK (World Bank, 2017). As is known, UK is one of the few G20 countries which has kept the pledge of providing 0.7 per cent of gross national income (GNI) as ODA. The provisional estimates for 2015 as presented in June 2016 (Lunn and Booth, 2016), and updated by the UK Government, suggest that UK has spent GBP 12.24 billion in ODA, which is 0.71 per cent of its GNI, and about 1.6 per cent of public spending.[35] UK continued this trend in 2016 as well, with the ODA-GNI ratio being 0.7. Net aid flow from the UK as a member of the OECD's Development Assistance Committee (DAC) was USD 200 million in 2016.[36]

Two issues are pertinent here. First, the capacity of UK to maintain its record as a major development partner will hinge on the performance of post-Brexit UK economy. Second, it will also be predicated on the policies to be pursued by post-Brexit governments. What has already emerged is that, the value in BDT of the aid received by various recipients in Bangladesh, be it the government or the private sector and non-government organisations (NGOs), and has seen significant reductions in Taka terms in the past year. Even if the UK continues to meet its ODA commitment (as was stated by Mark Matthews, UK representative to the United Nations Conference on Trade and Development (UNCTAD)), the amount will depend on the size of UK's GNI and the value of the GBP. EU-pooled aid and financing by the European Investment Bank (EIB) will also be affected significantly by Brexit. Particularly because, about 10 per cent of EIB investments are directed to developing countries, and UK is the biggest investor in EIB, holding 17 per cent of EIB capital. Thus, there is also considerable uncertainty as regards aid commitment during the post-Brexit UK and the role that the UK will play in multilateral organisations as a development partner.

5. CONCLUDING REMARKS AND POLICY RECOMMENDATIONS

Brexit comes at a time when Bangladesh has graduated (in 2015) from low-income to lower middle-income country (LMIC) status as per World Bank categorisation. Bangladesh has also become eligible for LDC graduation in March, 2018. The looming uncertainties as a result of Brexit referendum and their consequent impacts and implications ought to be carefully examined and weighed by Bangladesh's policymakers. With the formal Brexit negotiations going on in full swing, it is only logical that Bangladesh follows the upcoming Brexit negotiations with a keen interest in view of the traditionally strong ties that the two countries have developed over the years. UK is a key development partner of Bangladesh, and the ties between the two countries cover a wide range of areas—trade and commerce, business and investment, aid and development support, people-to-people contact. Thus, it is in Bangladesh's interest to remain engaged with the UK in view of the emerging scenario. Bangladesh's negotiations with the UK, on a bilateral basis or as part of the LDC group, must be informed by the likely adverse implications of Brexit on Bangladesh and other low-income economies. Bangladesh needs to develop an appropriate strategy to address the emergent concerns by pursuing a proactive policy in relation to the UK.

The preceding analyses reveal that, Bangladesh has reasons to be worried on account of the Brexit. Immediate impacts of Brexit on the currency market and the fall in the value of the GBP have had negative implications for Bangladesh in several areas: export, remittance and the amount of aid received. Bangladesh exchange rate policy should take into consideration the behaviour of currencies

[35] UK aid was USD 18.7 billion in 2015 (OECD, 2016b).

[36] USD 250 million in 2015 and USD 343 million in 2014, with the highest being USD 425.3 million in 2013 (since 1998).

of its key competitors. In view of the volatility, Bangladesh will need to strategise to keep its currency competitive. Bangladesh should also negotiate with the UK to take advantage of the new immigration policy which will be put in place once these are designed. Now may also be a good time to raise funds through issuance of GBP-backed bonds, perhaps to underwrite large scale infrastructure financing. Consultations may also be held with the UK Government with regard to safeguarding the value of aid money by hedging the currency (GBP) fluctuations. The currency market, though has somewhat returned to the normal after the initial volatile reactions, is yet to fully stabilise. It is conceivable that, there will be uncertainties till the time the Brexit deal is sealed. Forward looking strategies, for example hedging against currency fluctuations that were experienced following the Brexit referendum, are called for.

Bangladesh should start thinking about building a bilateral relationship with the UK on a new foundation in the backdrop of the Brexit referendum. Of key significance here will be post-Brexit trade relationship with the UK. Market access conditions, RoO, IPR regimes, SPS standards, technical barriers to trade (TBTs)—all these may need to be negotiated anew. It is likely that UK will not be part of the Single Market, but remain in the EU-FTA. In this case, one option is for the UK to coopt some version of the EBA. LDCs have a collective interest to continue to gain market access in the UK under the EBA terms. As a leading member of the LDCs, Bangladesh should exercise leadership in negotiations with the UK as regards this. There may be trade diversion if the UK is not in the European Customs Union, and this will need to be taken cognisance of. If UK decides to go for a separate trade deal, it will be in the interest of the LDCs to negotiate as a bloc, and for maintaining the EBA terms. Of critical interest will be to retain the RoO as stipulated in the EBA, particularly the prevailing one-stage RoO for exports of apparels applicable both for the knit and the woven items.

Bangladesh will hopefully graduate from the LDC status by 2024. Special treatment enjoyed by Bangladesh as an LDC will not be there in most of the partner countries after 2024. As is known, the EU has agreed to extend the EBA to graduated countries for additional three years. This means Bangladesh will receive market access to the EU under the EBA till 2027. UK may come up with a preferential scheme for the LDCs such as the EU GSP+. However, this type of preferential treatment will likely be provided only with stringent conditionalities.[37] As was noted earlier, the UK-Bangladesh trade channel is also used by Bangladeshi exporters and UK importers to send goods onward to other European countries. The future dynamics of this practice will depend on how the EU-UK trade deal is negotiated. Indeed, the supply chain with British retail brands importing goods from Bangladeshi producers, and then exporting onward to other European destinations, will be significantly impacted by the nature and content of the UK-EU trade deal and dynamics of changes in the UK-EU bilateral relations. It is in Bangladesh's interest to approach and negotiate with the UK a deal which takes care of all the details in this connection. UK can also decide to go for a Pan-Commonwealth trade pact. Bangladesh should play a leading role if such a deal is to be negotiated. One also hopes, that the UK will not deviate from its resolve to adhere to the aid commitment of 0.7 per cent of GNI.

UK investors in Bangladesh, a significant part of whose products are destined to the UK and EU, and who enjoy duty-free market access, will be watching the emerging scenario very closely. Any possibility of changes in market access conditions in the UK and the EU will be closely monitored by the current and potential investors (for instance, currency gains).

Brexit negotiations are likely to continue till March 2019 (and even beyond, subject to the concurrence of all the parties). It is quite early to speculate how the negotiations will evolve. UK is hoping to have a trade deal that will be significant in terms of 'scope and ambition', and it is keen to maintain 'deep and

[37]EU GSP+ requires beneficiary countries to ratify and strictly to implement and monitor the 27 ILO core labour standards.

special' relations with the EU. However, it is still uncertain whether it is going to be 'Hard Brexit' or 'Soft Brexit'. In view of the evolving scenario, it is suggested that, Bangladesh sets up a Task Force to study the possible impacts of Brexit on the Bangladesh economy, and to design appropriate strategies in this connection. The mandate of the Task Force may be (a) to study the terms of Brexit, its implications and ramifications, for Bangladesh (market access, RoO, standards, IPR regime, migration, remittance, investment, aid); (b) to examine the developments in the UK economy, their market demand situation and currency movements, and financial markets dynamics and their relevance for Bangladesh (BDT exchange rate and remittance flow); (c) to study UK's dealings in multilateral fora such as the WTO (adoption of schedule of concessions in the WTO, negotiations with other members, aid for trade commitments, etc.) and mega-regionals (likely regional trade agreements with UK participation, with US and other countries, their terms, preference erosion for Bangladesh, etc.); and (d) to provide strategic guidance to the Government of Bangladesh to build Bangladesh-UK bilateral relationship for the emerging post-Brexit era (trade and market access, investment, aid, migration—to name a few) as also to contribute to designing to Bangladesh's stance as a leading member of the LDCs, to help protect the benefits currently being enjoyed by the LDC group with respect to the UK.

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ANNEXES

Annex 1: The EU-Referendum Debate and Brexit Negotiations

Annex Table 1: Arguments For and Against the UK's Exit from the EU

Topic of Debate	FOR the UK's Exit from the EU (LEAVE)	AGAINST the UK's Exit from the EU (REMAIN)
Trading with the EU	UK will be able to strike more beneficial trade deals with EU, without having to compromise on sovereignty over policies and borders binded by EU laws.	Less than 8 per cent of EU exports come to UK, while 44 per cent of UK exports enter EU. Over one million UK businesses trade, without export or import charges or paperwork, in the EU market.[a]
Trading with non-EU countries	UK will be free to negotiate new favourable trade deals with countries such as the United States (US), New Zealand, Australia; and emerging economies such as Brazil, China and India.	As a member of the EU, UK is able to get better deals because of the strength and size of the Single Market that the EU offers. UK already enjoys advantageous trade deals as part of the EU.
Job opportunity or job loss	New opportunities will mean more job creation. Some pro-exit experts felt that job losses will be more than compensated by stimulating the financial sector; flexible regulations will lead to job creation.	Over four million UK jobs are linked to trade with the EU.[b] Up to 950 thousand UK jobs could be lost by 2020 as a consequence of Brexit on the UK economy.[c]
Contribution to EU-spending	UK will be able to make savings on the budgetary contribution to the EU, which can then be deployed to cater to its own priority requirements like health, education, scientific research, new industries and housing.	Net benefit of being in the EU was worth GBP 62-78 billion per year. Leaving the EU will lead to significant erosion in the quality of public services. Additionally, crucial EU funding for research and development will be lost.
Freedom from EU rules and regulations	Exit from the EU will help the UK regain sovereignty and get greater control over monetary, financial and economic development policies.[d]	EU rules and regulations combine 28 national standards to constitute more unified EU standards. This greatly facilitates conducting business in the Single Market and cooperation among member countries.
Control over borders and immigration	UK will reclaim its borders. It will be able to control and deploy discretionary measures as regards access of immigrants to the UK based on skills, rather than countries of origin. Thus, UK will be able to treat EU and non-EU immigrants within common frameworks.	UK has complete control over the entry of immigrants since it is out of the Schengen visa-free border area. However, UK enjoys the advantage of visa-free entry to the EU. Also, the number of EU migrants is relatively higher in other countries of European Economic Area (EEA) and European Free Trade Area (EFTA), compared to the UK.
Global influence	According to the Euro-skeptics, UK has insignificant influence within EU. Being outside the EU, UK will be able to represent itself more prominently at international institutions and negotiations, and will be able to more forcefully influence global policies relating to free trade and global cooperation.	UK's global influence will diminish if it leaves the EU. As part of the EU, UK is represented twice in international summits—at the level of UK ministers and concerned EU officials. This offers UK a better opportunity to influence various negotiations, including those relating to climate change regulations and global economic and political issues.

Source: Authors' compilation of information in Britain Stronger in Europe (2016); Great Britain (2016); Lilico (2016); Vote Leave (2016).

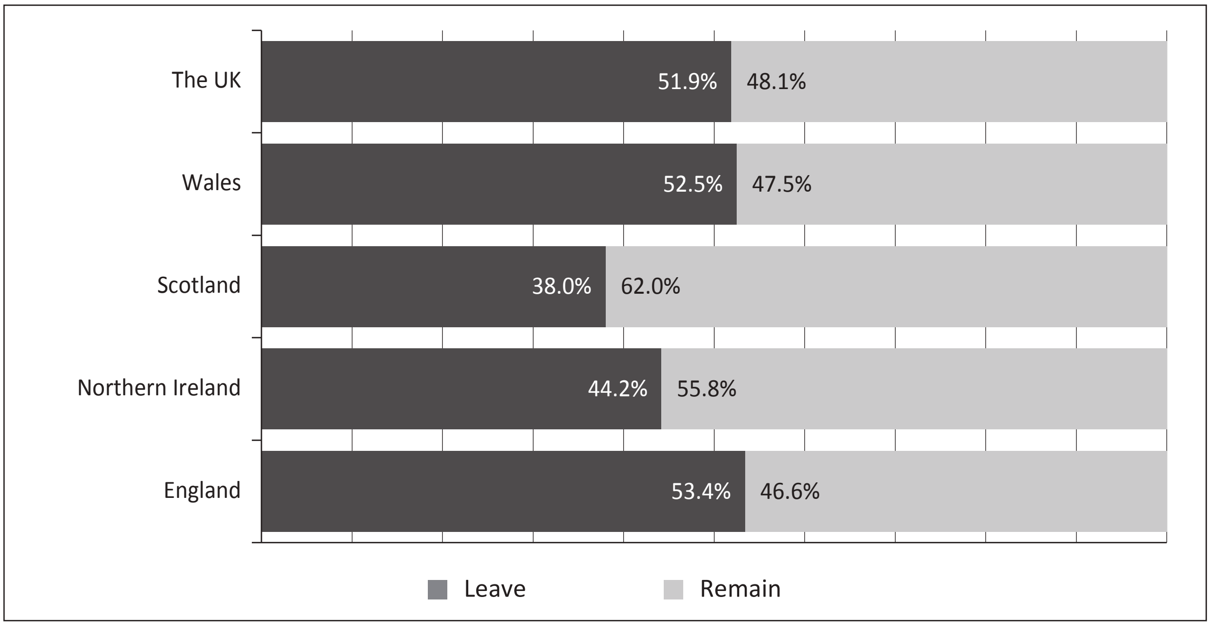
Note: [a] Great Britain Treasury (2016).

[b] Analyses by CEBR (2014) and O' Leary (2016).

[c] Analysis by Confederation of British Industry and PricewaterhouseCoopers (2016).

[d] Some prominent regulation parameters are—common product standards, similar health and safety standards, similar employment rights, and EU-wide sector-specific legislations.

Annex Figure 1: Britain's Nation-wise Results of the EU-Referendum



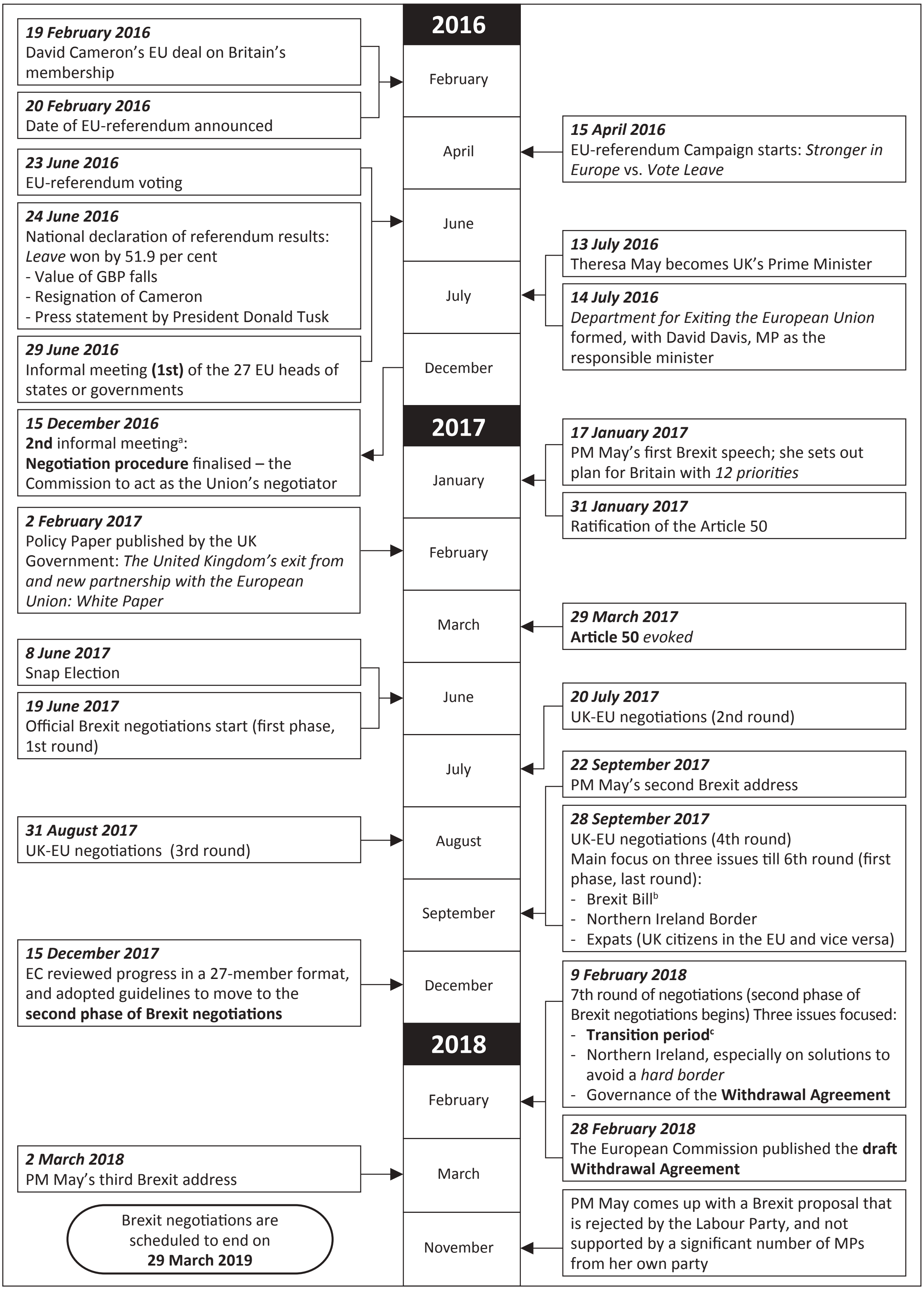
Source: The Electoral Commission (2016).

Annex 2: Key Brexit Milestones from Referendum to Negotiations

Following the ruling of the highest court that Parliament's voice is to be sought, the Brexit Bill was put to vote. The results of the referendum were overwhelmingly endorsed in the UK Parliament[38] on 31 January 2017, and the Article 50 was ratified. This vested Prime Minister May with the power to invoke Article 50 which she did on 29 March 2018; thus began the long process of UK-EU negotiations. The negotiating teams reached the end of the first phase of negotiations with significant outcomes on a number of important issues, and these were published as the Withdrawal Agreement. Prime Minister May has already endorsed the idea of leaving the Single Market and the customs union, and has recognised the significant trade-offs involved. In the coming days, the contours of the deal will become clearer. Annex Diagram 1 presents some key milestones of the Brexit negotiations.

[38]In the House of Commons, 498 members of Parliament (MPs) voted for the EU (Notification of Withdrawal) Bill, and 122 MPs voted against it, giving the Prime Minister May the power to trigger Article 50.

Annex Diagram 1: Selected Milestones Preceding and Following the EU-Referendum and Brexit Negotiations



Source: Authors' compilation based on GOV.UK (n.d.a); European Council (n.d.).

Note: [a] EU 27 country heads and Presidents of the European Council and Commission issued the statement on the decisions of the meeting.

[b] Though no specific figure is given in the documents, it is speculated to be between EUR 35 to 60 billion (inclusive of budget contributions during transition period).

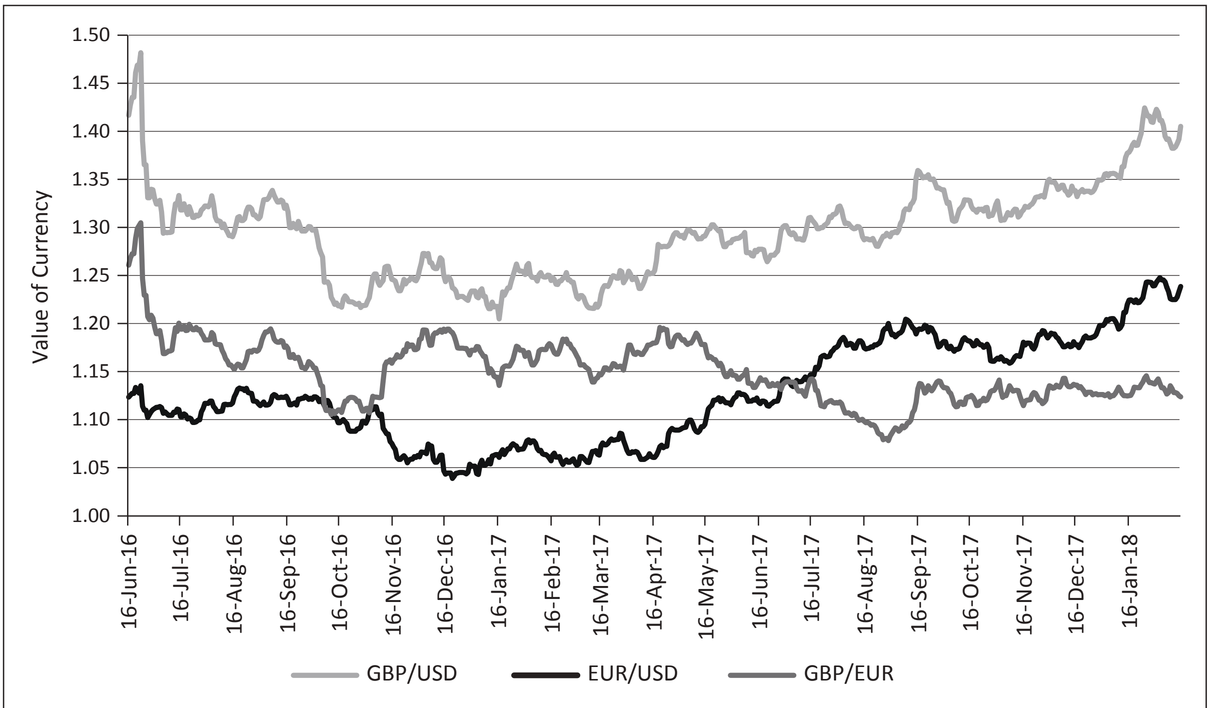
[c] EU has set the transition period up to 31 December 2020. Therefore, complete BREXIT will take effect in January 2021.

Annex 3: Short-term Impacts and Growth Forecasts for the UK Economy

Immediate fallouts of the EU-Referendum

- As the Annex Figure 2 shows, the strength of GBP experienced a decline in value (not seen before) against USD, EUR and other major currencies.

Annex Figure 2: Value of GBP/USD, GBP/EUR and EUR/USD



Source: Authors' calculation based on the exchange rate data obtained from Oanda (n.d.).

- The financial market experienced the onset of high volatility with Financial Times Stock Exchange (FTSE) 100 and FTSE 250, losing value significantly immediately after the vote. Asian, European, and thereafter the US share markets, faced a downward spiral of sell-off following the referendum. The market was caught by surprise by the Leave result and a record USD 2 trillion was wiped off the value of global shares (Wearden and Fletcher, 2016).
- FTSE 100 dropped by 8 per cent initially on 24 June 2016, but a full comeback on 28 June 2016, ending at 0.3 per cent higher than that on the referendum day. It made a speedy recovery as it contains companies which have wide-ranging international operations outside the UK, and was benefitted by the plunge of GBP value. On the contrary, FTSE 250 which includes relatively more UK-based companies, experienced a deeper loss and needed more time to recover (London Stock Exchange, n.d.).
- The post-referendum financial market reflects that a number of property-related equities were also adversely affected, in the same manner as FTSE 100 and FTSE 250 (Baker *et al*., 2016).
- Moody's (a credit rating agency) lowered debt outlook for the UK from stable to negative and reduced UK's AAA rating (highest) to AA+ (second highest).
- Demand and price of UK government bonds (gilts) rose sharply with consequent fall in yield. On 24 June 2016, the UK 10-years bond yield fell by 0.29 basis points, and as observed by Baker (2016), 10-years bond yield for Germany and France also fell in tandem, by 0.16 and 0.06 basis points, and that of Italy and Spain rose by 0.15 and 0.17 basis points respectively.
- Gold prices jumped by 8 per cent on the day after the referendum. Gold once again proved its worth as the preferred store of value in the face of uncertainty (Harvey and Nicholson, 2016).

- Housing market activity in the UK slowed down notably after the Brexit (RICS, 2016).

Official economic data published by the Office for National Statistics (ONS) in August 2016 gave some indication of the recovery (ONS, 2016):

- Employment rate rose to 74.5 per cent in May-July 2016 period; there were 39 thousand fewer unemployed people at that time compared to the period of February–April 2016.
- Retail sales increased by 1.6 per cent in value (amount spent) and 1.4 per cent in quantity compared to June 2016.
- Inflation rose from 0.5 per cent in June to 0.6 per cent in July, highest in 20 months.

Bank of England announced an economic stimuli package in response to the shock induced by the EU-referendum result (Bank of England, 2016).

- The interest rates were slashed from 0.5 per cent to 0.25 per cent in an attempt to stimulate investment, thus lowering the cost of borrowing for the first time since 2009.
- An additional GBP 70 billion was allocated as part of the quantitative easing programme, purchasing bonds—both corporate and government—and opened the window of a 'term funding scheme' worth GBP 100 billion to help banks transfer the benefits of lower interest rate to commerce and business.
- Moreover, after the quantitative easing measures were announced, the yields on gilts plunged even lower—the yield on 10-years gilts fell 15 basis points, and that of the 2-years gilts fell by 8 basis points (4 August 2016). This rise in demand for bonds as a safe haven, notwithstanding the reduction in the interest rates by the Bank of England, is indicative of the pessimistic economic outlook maintained by many.

Annex Box 1: Growth Forecasts for the UK Economy according to Research Results

International Monetary Fund (IMF) in World Economic Outlook released in July 2016 **(IMF, 2016a)**
▪ Lowered global growth forecast by 0.1 percentage point (from 3.2 to 3.1 per cent) for both 2016 and 2017 (from 3.5 to 3.4 per cent). ▪ UK's growth forecast was revised downward by 0.2 per cent (down to 1.7) for 2016, and by 0.9 per cent (down to 1.3) for 2017. In the outlook for the UK economy, IMF forecasted the gross domestic product (GDP) growth to be 1.5 per cent in 2018 (lower by 0.1 percentage point form 2017) suggesting Brexit uncertainties will weigh down. ▪ Growth forecasts for emerging and developing economies have been kept unchanged. This was reduced by 0.9 percentage points (for 2016) and 0.4 percentage points (for 2017) for low-income developing countries.
Asian Development Bank (ADB) in a supplementary release to Asian Development Outlook 2016 **(ADB, 2016)**
▪ ADB forecasts are for developing countries to grow by 5.6 per cent in 2016, slightly below the 5.7 per cent, considering the EU-referendum impacts. For 2017, growth was kept unchanged at 5.7 per cent. This was to be driven mainly by growth of India (7.4 per cent) and China (6.5 per cent) in 2016.
Organisation for Economic Co-operation and Development (OECD) in its Interim Economic Outlook **(OECD, 2016a)**
▪ Global GDP growth projected to remain flat around 2.9 per cent in 2016 (to rise to 3.2 per cent in 2017). ▪ Euro area growth outlook is 1.5 per cent in 2016 (1.4 per cent in 2017), revised down by 0.1 percentage point considering the spillovers of the EU-referendum. ▪ Growth projection of the UK has been revised upwards by 0.1 percentage point to 1.8 per cent in 2016. For 2017, GDP is projected to slow down to 1 per cent. This was revised downward by 1 percentage point considering the uncertainties relating to the future policy trajectory.
Capital Economics Limited **(Capital Economics, 2016)**
▪ UK will possibly face modest negative impact as regards growth and job creation.

Annex 4: Econometric Analysis of the Implications of Brexit on Bangladesh's Exports

An augmented gravity model was used to estimate the impact of Brexit on Bangladesh's exports. Several studies have deployed gravity type of model to analyse the importance of EU membership for the UK's economy, in view of the EU-referendum. Results of the various models presented in several papers reveal the significant positive impact of EU membership on trade (Fournier *et al*., 2015; Great Britain Treasury, 2016; IMF, 2016b), and on FDI received by the UK (Bruno *et al*., 2016; Great Britain Treasury, 2016). The current analysis examines the economic ramifications of Brexit specifically for exports of Bangladesh.

The study uses a fixed and balanced panel data framework. Annex Table 2 presents data, definition and sources. The panel is arranged across 58 countries[39] for 25 years (1991 to 2015). The total number of observations is 1,450. The analytical framework offered by the panel data helps to understand the relationship of the explanatory variables and the dependent variable over time, separating it from the possible effects of time-specific and individual-specific factors. In the regression model, Bangladesh's annual export data for selected 58 countries have been taken as a dependent variable. As explanatory variables, the standard gravity model variables—incomes of both trading partners, contiguity of the border between the trading partners, the presence of common language, the distance between Dhaka and the capital of partner countries, were taken. This general gravity model was then augmented by using the explanatory variables—real exchange rate, tariff rates faced by Bangladeshi exports and EU dummy (takes the value of 1, if the importing country is a member of the EU at the considered time period, otherwise zero). These are the three objective variables for this particular analysis.

Panel data estimations were carried out in the study by using the pooled ordinary least squares (OLS) regression, random effects model (REM), fixed effects model (FEM) and PPML estimation techniques. On the basis of post-estimation results (after controlling for heterocedasticity, multicollinearity, model specification test) the specified models discussed in the paper were found to be best explained. The study has run the REM, and then carried out the Breusch-Pagan Lagrangian Multiplier test for testing the presence of random effects. Rejecting the null hypothesis of the test (H_o: The individual or time-specific error variance components are zero), the data confirms to have individual or time-specific effects. If these individual effects are random and not correlated with the explanatory variables, then REM is preferred, however, if they happen to be correlated with the explanatory variables, then FEM needs to be employed to capture the net influences of the explanatory variables. This distinction is done by the Hausman specification test, in which the rejection of the null hypothesis (H_o: No correlation between the individual effects and the regressors) suggests preferring the FEM. Once FEM was chosen and tested by the F-test, the study has run the Least Square Dummy Variable (LSDV) model to correct for the characteristic inability of FEM to estimate time-invariant variables like distance, contiguity, etc. Moreover, it was observed in the results that, LSDV model improves all the measures of the goodness-of-fit like F-test, R^2, etc., and absorbs the individual or time-specific effects. The study has controlled for dyadic fixed effects and time dummies.

[39]The top 58 export destinations based on the export figures of FY2015-16 (EPB, 2018).

Annex Table 2: Data Definition and Sources

Variable	Description	Unit	Source
export volume $_{ij,t}$	Exports from Bangladesh (*i*) to importing country (*j*)	Million USD	Trade Map (n.d.)
GDP $_{j,t}$	GDP of importing country	USD	World Bank (2017)
GDP $_{i,t}$	GDP of Bangladesh	USD	World Bank (2017)
GDPPC $_{j,t}$	GDP per capita of importing country	USD	World Bank (2017)
GDPPC $_{i,t}$	GDP per capita of Bangladesh	USD	World Bank (2017)
population $_{i,t}$	Population of Bangladesh		World Bank (2017)
population $_{j,t}$	Population of importing country		World Bank (2017)
distance $_{ij}$	Geographical distance between the capitals of the two trading countries	km	CEPII (n.d.)
contiguity	This is a dummy variable which takes the value of 1, if the trading countries have common border	0, 1	CEPII (n.d.)
tariff $_{j,t}$	Applied tariff rate of importing country	per cent	World Bank (2017)
eu $_{dummy}$	Dummy variable which takes the value 1, if importing country is an EU member	0, 1	European Union (n.d.)
$RERE_{i/_{j},t}$	Real exchange rate with Euro incorporated. It shows the amount of BDT available per unit of importing country's currency (LCU—Local Currency Unit)	BDT/LCU	Authors' calculation
tcost $_{ij,t}$	This is the ad valorem trade cost between country *i* and country *j*	per cent	ESCAP-World Bank (n.d.)

The variable $RERE_{i/_{j},t}$ has been calculated using the following formula as used by Khatoon and Rahman (2009):

$$RER_{i/_{j},t} = E_{i,t}\left[\alpha_{j,t}\left\{\frac{CPI_{j,t}/(e_{j,t})}{CPI_{i,t}}\right\}\right]$$

Here,

$RER_{i/_{j},t}$ = Real exchange rate (BDT/LCU) in time period *t*

$E_{i,t}$ = Nominal exchange rate of Bangladesh's (*i*) currency against USD (BDT/USD)

$\alpha_{j,t}$ = Trade ratio of country *j* in year *t* = $\frac{trade\ with\ country\ j\ in\ year\ t}{total\ trade\ in\ year\ t}$

$CPI_{j,t}$ = Consumer Price Index (CPI) of country *j* in year *t*

$e_{j,t}$ = Nominal exchange rate of importing country *j*'s currency against USD (BDT/USD)

$CPI_{i,t}$ = CPI of Bangladesh in year *t*

As is known, the European common currency, the Euro, was introduced as a Europe-wide medium of exchange (though not all EU members joined the move). To address this change, real exchange rate of EUR against BDT has been incorporated in the equation, and the new variable $RERE_{i/_{j},t}$ has been introduced.

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