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Ten Years After Brexit:
Resilience Without Revival

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Content

Executive Summary


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- **Brexit 10 years on: Neither collapse, nor renaissance.** As the UK looks for its 7th Prime Minister in 10 years, this week also marks a decade since Brexit roiled markets and divided forecasters. Predictions ranged from economic collapse to a renaissance. A decade later, we take a hard look at which projections came through and which failed to pass. The outcome has been more nuanced that many expected, with indicators pointing to both economic strengths and weaknesses — not all of them Brexit related.
- **Britain's Economic Backbone: The knowledge economy, tech and clean energy.** UK ICT exports to the EU have almost doubled since Brexit, demonstrating the continued competitiveness of Britain's knowledge economy. The UK remains the world's second-largest exporter of financial services, accounting for 21% of global exports, while deepening its provision of financial services to EU markets. In private markets, the UK continues to attract more venture-capital funding than any European competitor. Between 2020 and 2026, it raised roughly USD164bn. Since then, London has retained much of its global financial importance. The UK still accounts for nearly 50% of global OTC interest-rate derivatives trading and almost 38% of global foreign-exchange turnover. In clean energy, the UK has emerged a leader within Europe. Wind generation has increased by 130% since 2016, reducing the UK's fossil dependence while enabling a successfully phased out coal in 2024.
- **Burned by Brexit: Dragging growth, trade frictions and lagging Leavers.** Independent studies estimate that GDP would have been 2 to 4% larger without the political instability and trade friction triggered by Brexit. Since 2016, "Leave" regions have generally underperformed compared to the UK as a whole: 59% of the population of the ''Leave'' areas have seen their regions fall further behind national income per capita average. Since the vote and the formal exit from the bloc's economic structures on 1 January 2021, growth has relied increasingly on foreign-born workers, which has fueled more than half of GDP expansion. Brexit has increased frictions and reduced trade flows. While the EU remains the UK's largest trading partner, structural estimates suggest UK-EU trade is around 21% lower for goods than it would have been without Brexit. New trade agreements and diversified supply chains with the US, China and Commonwealth countries have failed to match the scale of the economic ties previously enjoyed within the EU. UK assets continue to trade at a discount relative to international peers.
- **A lasting lesson of the 2022 mini-budget crisis is that fiscal credibility**

matters. Investors now demand a structurally higher risk premium on UK assets against a backdrop of rising fiscal imbalances. Equity markets, where UK stocks have underperformed both US and European peers in the past decade, reflect this premium. In private markets, the magic has faded into a priced-in discount. A decade on, Brexit's imprint reads through the UK's two largest private-capital engines, private equity and venture. UK investments were 12–18% below a no-Brexit path as of 2025, a one-off level shift now cleared into a structurally higher cost of capital. Private equity has proved resilient, but increasingly as a US funded value trade rather than home grown momentum with compressed valuations turning UK companies into take-private targets for US capital.

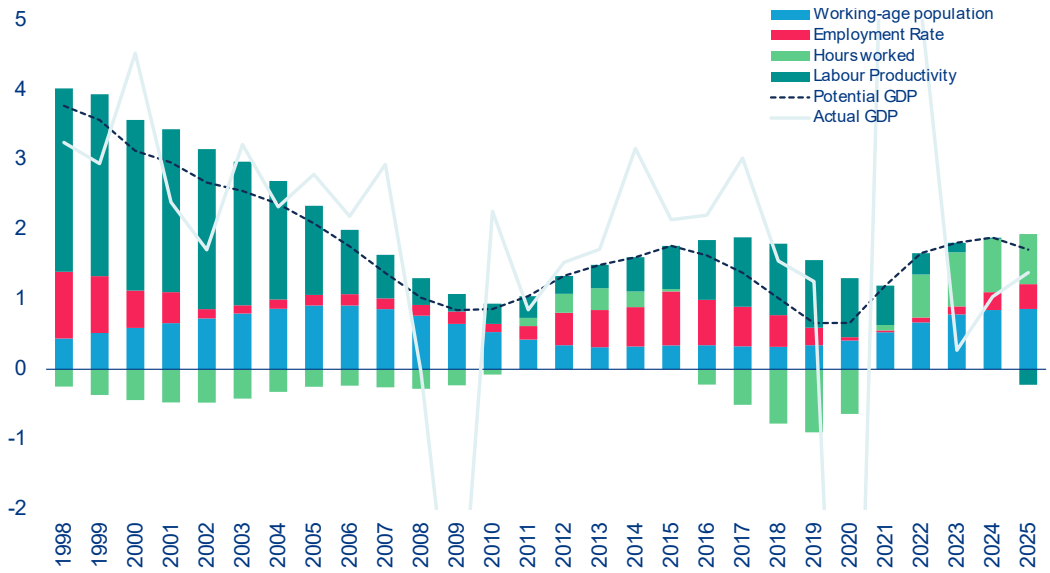
- **Beyond Brexit: Identifying and implementing solutions for the future.** The UK scores high on business creation, labor-market flexibility, higher education and research, compared with many other advanced economies. This indicates that domestic bottlenecks — exposed by Brexit but not caused by it — are the root of the country's disappointing growth performance. The government has identified many of these issues, but needs to push further. Priority actions should include:
  - Accelerating planning reform,
  - Increasing investment in housing and energy infrastructure,
  - Strengthening support for innovation and strategic industries,
  - Treating NHS reform as an economic priority, and
  - Addressing the slow diffusion of new technologies from frontier firms to the broader economy.
- **A revamp of fiscal rules, combined with reforms to pensions spending and property taxation as well as broadening the VAT base, would help redirect scarce public resources toward deficit reduction and investment, with an eye to defense.** Unlike the EU-27, Britain has staged no distinct post-2022 rearmament inflection. The UK government has committed to increase defense spending to 2.5% of GDP by April 2027, and 3.0% target by 2030, but they are not set in stone. The cooperation map looks busy — AUKUS with the US and Australia, GCAP with Japan and Italy, a privileged-partner track toward the EU's SAFE instrument — yet it reads as a catalog of commitments rather than tangible delivery. Government investment would help attract investors and domestic defense companies to commit capital to UK capacity. Reintegrating more closely with European energy markets would generate meaningful economic benefits. High energy prices caused by the UK leaving the EU Internal Electricity Market, successive energy supply crises and grid bottlenecks linked to the rapid expansion of renewable energy have continued to undermine industrial competitiveness. Divergence between UK and EU carbon markets also risks creating new trade barriers for energy-intensive industries. Reintegrating energy and carbon markets cancould help to reduce friction costs, stabilize power prices and improve supply security.

10 years since the Brexit vote: an evolving economic and energy landscape

This month marks 10 years since the Brexit vote and the promises of greater democratic accountability, reduced immigration and independent trade policy. The Brexit referendum took place on 23 June 2016, gathering a high turnout of 72.2%, with 51.9% (17.4mn) votes for leaving the EU against 48.1% (16.1mn) for remaining. The Leave campaign was built around several core themes and promises. First, sovereignty, or"Take Back Control": restoring the authority of the UK Parliament by removing the influence of EU institutions and courts. Second, immigration control: ending the free movement of people from the EU, and allowing the UK to set its own immigration policy. For most Brexiters, this meant reducing the flows of immigration drastically, including from non-EU countries. Third, trade and regulation: gaining the freedom to negotiate independent trade agreements and reducing or removing EU-derived regulations. Fourth, budget contributions: stopping contributions to the EU budget and redirecting some of those resources to domestic priorities (notably providing additional funding to the NHS). Finally, democratic accountability: decisions affecting the UK would be made by elected British politicians rather than EU bodies. In all, Leave supporters generally argued that Brexit would increase political autonomy and economic flexibility, while opponents warned about trade barriers, lower investment and weaker economic growth. The UK effectively left the EU on 31 December 2020.

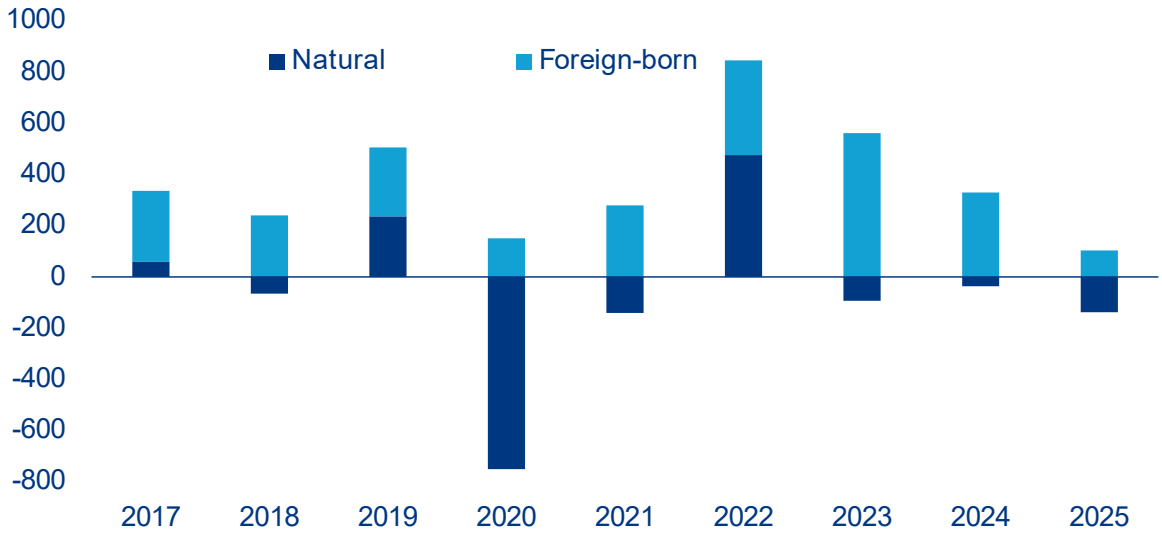
UK politics has been shaken since the 2016 vote. Debates about closer ties with the EU, or even potential re-entry into the EU, have gained momentum recently amid a Labour party leadership contest. The post-Brexit period has been one of unusually high political turnover in the UK. Since the referendum, the UK has had six Prime Ministers (PM), compared with only four PMs during the entire 1997-2016 period. Much of this high turnover was directly linked to Brexit negotiations, disagreements over the UK's future relationship with the EU and subsequent political pressures. Poor fiscal decisions against a backdrop of rising budget imbalances added to the political instability, with the infamous ''mini Budget'' debacle of unfunded tax cuts by PM Liz Truss and Chancellor Kwarteng in September 2022 spooking financial markets. The recent challenge of PM Starmer's leadership with the ruling Labour Party has sparked a renewed debate over the opportunity to deepen trade and economic ties with the EU. The current government's stance is to rule out rejoining the customs union or the single market or bringing back freedom of movement.

Figure 1: Potential GDP growth decomposition (% y/y, left)



Sources: LSEG Workspace, Allianz Research

Figure 2: Employment growth decomposition (000s, right)



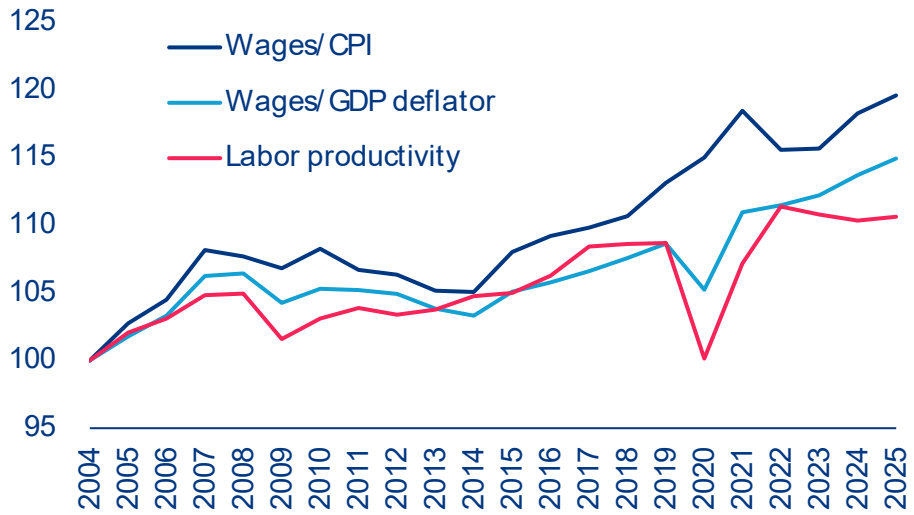
Sources: LSEG Workspace, OECD, Allianz Research

Note: we take into account only permanent migration, which is defined by legal status, not duration of stay by the OECD. It includes migrants with a pathway to remain indefinitely such as refugees, family migrants and some labor migrants, while those without such rights (e.g. students or seasonal workers) are not considered. As per the OECD estimate, we assume that roughly 75% of new immigrants to the UK become employed.

Reduction of regional economic disparities has been disappointing. While Scotland and London strongly supported remaining within the EU, other regions such as the Midlands and North East of England voted firmly to Leave. Reducing inequalities across regions, was a key talking point both during and after the Brexit referendum. ONS data indicates that convergence has generally failed to materialize. We look at the sample of 332 areas in Great Britain representing over 61 million people. 227 areas voted Leave and 105 voted Remain. 59% of the population of ''Leave'' areas have seen their regions fall further behind national income per capita average since 2016, although some important leave-voting cities such as Blackpool, Doncaster and Wolverhampton have seen an improvement compared to the UK average.

GDP growth has held up since Brexit, but shifted towards more government consumption and less business investment. Higher immigration flows and working hours per worker have offset worsening productivity trends. Despite the challenging environment since Brexit, including the Leave vote, ''Truss'' moment, political instability, Covid pandemic and energy shock of 2022, UK GDP growth has held up well. Annual GDP growth averaged +1.4% since 2016 — exactly the same average pace than the previous 10 years (2005-2015). The composition of growth changed, however, with higher growth of government consumption (+2% vs +1.3%) and residential investment (+3.6% vs -1.8%) offsetting lower business investment growth (+2.4% vs +3.7%). Export and import volumes both decelerated at roughly the same pace (-0.7pp to +2.5% for imports, -0.5pp to +2.4% for exports). Household consumption growth was unchanged (+1.3%). From a supply-side perspective, the underlying drivers of potential/sustainable GDP growth[1] changed even more dramatically. The working-age population re-accelerated after 2016 (Figure 1), supporting job creations and GDP. Job creation remained concentrated among foreign-born workers (newcomers) (Figure 2), amid worsening demographics for native and longer-term residents. In all, foreign born workers' jobs have grown +0.8% per year on average since 2016, contributing to more than 50% of UK GDP growth[2]. Meanwhile, trend growth of hours worked per worker has also accelerated, whilst trend productivity growth faltered. In all, while UK GDP growth has been resilient since Brexit, studies generally estimate that in a counterfactual were Brexit not to happen, GDP would have been between +2% and +4% larger[3].

Figure 3: Labor productivity & real wages (indexed 100 in 2004)



Sources: ONS, Allianz Research

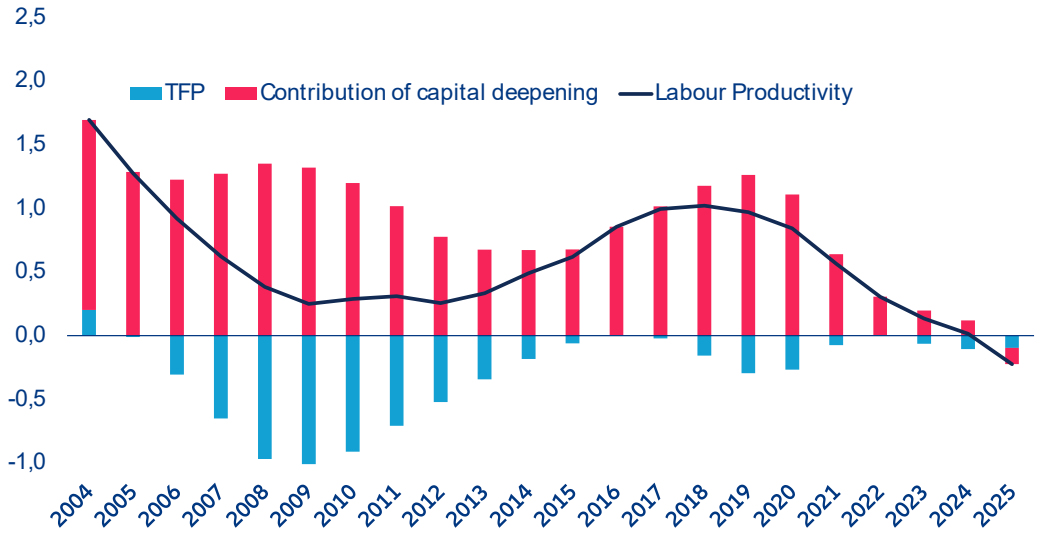
1 We look at potential GDP to strip out cyclical and financial effects that could blur the analysis.

2 Immigrants may generally have lower productivity levels than the rest of the population in aggregate (because they tend to work in lower-paid sectors), and therefore weigh on productivity dynamics and GDP growth by this channel. As a result, we take a conservative estimate (50%) lower than headline employment numbers would imply (57%).

3 For instance the Bank of England estimates a cost of -3.5% GDP.

Real wages and income growth has been decent despite an inflation surge, but poor productivity is likely to increasingly weigh on prospects. Real income per capita and wage growth have picked up pace since Brexit, despite continued poor productivity performance and elevated inflation. Real income per capita has grown by +0.9% per year on average since 2026, against +0.5% in the ten years prior. Real wage (adjusted by CPI inflation) trends showed even better improvements (+0.9% vs. +0.1%). But this occurred against a backdrop of lingering productivity weakness, which has increased in importance since the pandemic (Figure 3), signaling increasing margin compression for corporates. In other words, decent real wage (and income) growth is unlikely to last unless productivity picks up and/or corporates continue to take the hit on their margins. Very slow investment and capital accumulation has intensified since the pandemic, increasingly weighing on trend productivity growth (Figure 4). The persistent weakness of total factor productivity (TFP), i.e. the underlying efficiency of the economy, reflects many factors that are common to many other developed nations. Recent analysis suggests the slower diffusion of new technologies from frontier firms to the broader economy has been a key impediment to TFP[4].

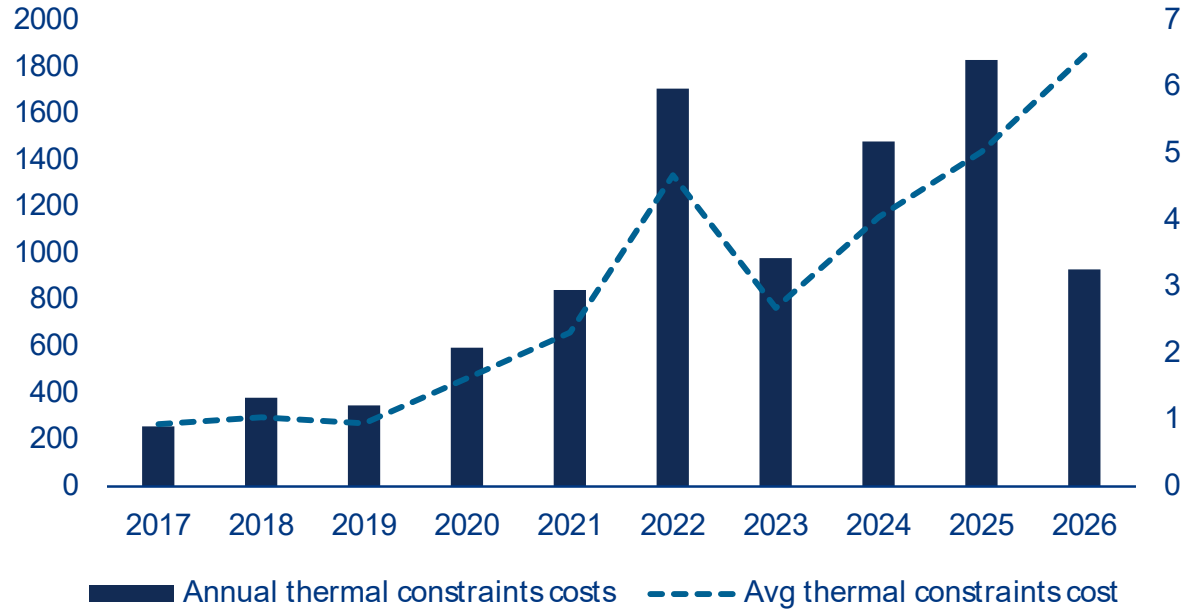
Figure 4: Trend productivity growth decomposition (% y/y)



Sources: LSEG Workspace, Allianz Research

4 The basic idea comes from a series of OECD papers by Dan Andrews, Chiara Criscuolo and co-authors. They show that productivity growth at the global frontier remained relatively strong during the 2000s and 2010s, but that the gap between frontier firms and the rest of the economy widened. In other words, innovation did not stop; the problem was that innovations spread more slowly to ordinary firms.

Figure 5: Annual thermal grid constraints/congestion costs in the UK power grid (in EUR mn, left) and average daily costs



Sources: LSEG Workspace, Allianz Research

Sector-wise, some services activity (transport and storage, ICT, support services activities, professional services) and public administration output have done well, Manufacturing flatlined but with some bright spots. Structural changes since the pandemic, including global ones, such as increasing Chinese competition on manufacturing, have likely played more of a role in shaping economic outcomes than Brexit itself. The UK manufacturing sector was -1.4% lower in 2025 relative to 2016. However, this masks dramatic shifts within the industrial sector, with energy-intensive sectors shrinking and less energy-intensive sectors doing well. Transportation equipment (+25% between 2025 and 2016), pharmaceuticals (+43%), textiles (+8%), agrifood (+31%), electrical equipment (+20%) and computer & electronics (+20%) saw a sharp increase of production. Meanwhile food/paper (-11.7%), coke/refined petroleum products (-38.4%), chemicals (-10%) and gas steam/electric output (-54%) shrank dramatically.

On energy markets, the UK's departure from the EU Internal Electricity Market (IEM) on 1 January 2021 is one of the most direct and measurable Brexit-related costs for UK energy consumers. Under IEM market coupling, interconnectors used implicit capacity allocation to converge prices efficiently across borders. After Brexit, the shift to explicit auctions reduced trading efficiency and increased transaction costs, resulting in an estimated upward pressure on wholesale prices of between 0.25-0.7% (GBP90-250mn) in 2021[5]. The UK also lost its previous role in EU electricity-market governance and ENTSO-E decision-making structures, although operational cooperation between British and continental system operators remains extensive.

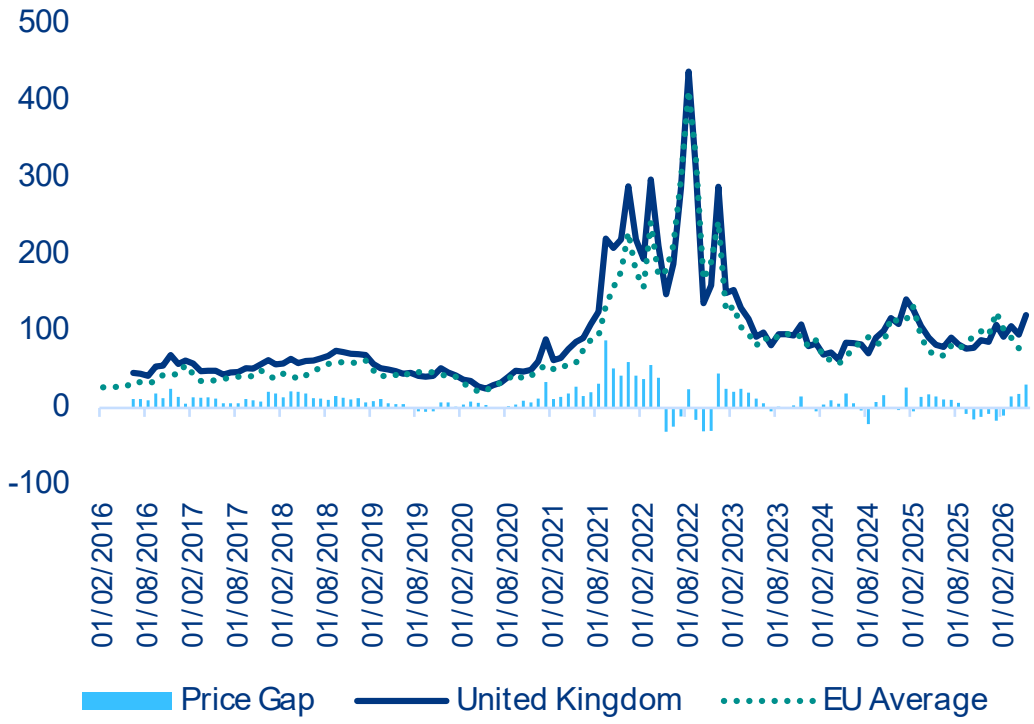
5 UK-EU Energy and Climate Cooperation: Why heightened engagement is imperative for Net Zero (Energy UK)

These institutional changes coincided with a broader structural evolution of the UK electricity system. Wind generation has more than doubled since 2016 (+130%), while solar output has increased by 85%, marking a rapid expansion of variable renewable capacity. This transformation enabled a landmark milestone: the UK completed its coal phase-out in September 2024, becoming one of the first major economies to eliminate coal from its electricity system entirely.

However, the rapid expansion of renewable generation has been highly geographically concentrated, particularly in northern Scotland, creating a growing imbalance between generation and demand centers. This has resulted in a severe north–south transmission bottleneck with rapidly escalating system costs. Thermal constraint costs, the cost of managing congestion in the electricity grid when power cannot be transported from where it is generated to where it is needed, rose from GBP258mn in 2017 to GBP1.83bn in 2025 (Figure 5). Based on the H1 2026 run-rate of GBP6.5mn per day, full-year 2026 costs are on track for approximately GBP2.4bn (+29% year-on-year). While these costs are primarily driven by domestic grid constraints and the spatial distribution of renewable generation, rather than Brexit itself, Brexit remains relevant in a second-order sense. Reduced integration with neighboring electricity markets and slower progress towards coordinated North Sea infrastructure may have limited the system's ability to alleviate congestion through cross-border balancing and joint offshore grid development.

The UK has materially benefited from cross-border electricity trade, with interconnectors enabling imports of lower-priced continental electricity and reducing the need for domestic redispatch. This is reflected in a close relationship between UK–EU price differentials and physical flows, with the UK typically acting as a net importer when domestic wholesale prices are below those in neighboring EU markets (Figure 6). This mechanism also helps reduce price volatility by allowing continuous arbitrage across markets. In 2022, however, this relationship temporarily reversed: the European energy crisis and reduced French nuclear availability tightened continental supply conditions, leading the UK to become a net exporter as flows adjusted to extreme price differentials.

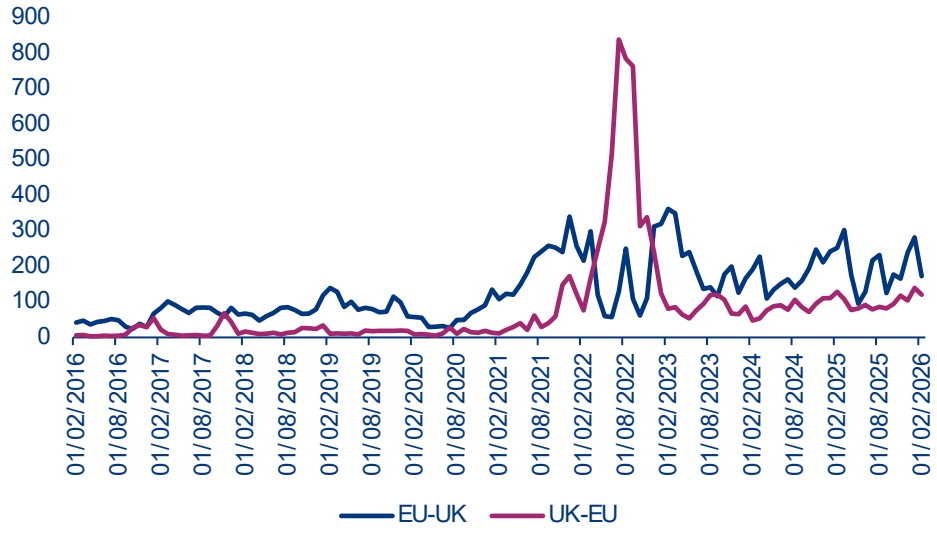
Figure 6: UK vs EU power price development and gap (USD/MWh)



Sources: EMBER, Eurostat, Allianz Research

By contrast, the widening of the UK–EU electricity price gap in 2021–22 reflected a period in which both domestic flexibility and cross-border trading efficiency were reduced. This included the IFA1 interconnector outage, an unusually low wind year in Great Britain, increasing reliance on gas-fired generation and reduced interconnector efficiency following the post-Brexit shift from implicit to explicit capacity allocation. Together, these factors increased the decoupling of UK and EU power prices during the initial post-Brexit period and subsequent energy shock. As a result, the post-Brexit UK electricity price premium over the EU rose by 23.6%, peaking between September 2021 and May 2022, when UK wholesale prices averaged EUR52/MWh above the EU average. Although this premium has partially normalized, it remains structurally elevated at EUR15–25/MWh in 2024–25, reflecting persistent integration frictions and a higher reliance on domestic gas-fired generation.

Figure 7: Cross-region power trade (EUR mn, right)



Sources: EMBER, Eurostat, Allianz Research

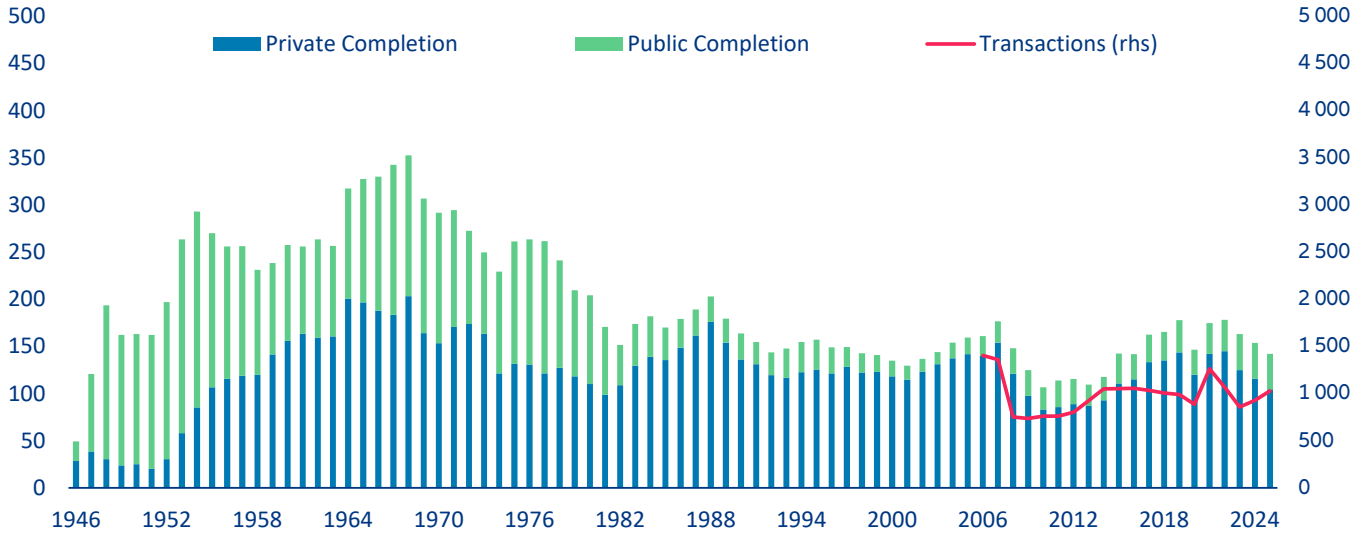
Figure 8: Co-development of UK and EU ETS allowance prices (in EUR/tCO2)

Sources: LSEG Workspace, Allianz Research

While post-Brexit divergence in energy markets has remained relatively limited, carbon pricing is emerging as a potentially more material channel of separation through its impact on trade-exposed industrial costs. The UK ETS has traded at a persistent discount to the EU ETS since 2023 (Figure 8). This reflects weaker allowance demand in the UK power sector following rapid decarbonization and greater policy uncertainty around the future tightening path relative to the more clearly signaled trajectory of the EU system. While this reduces compliance costs for UK emitters, it weakens the relative carbon price signal and creates a growing competitiveness gap for energy-intensive sectors exposed to European markets.

This gap becomes more consequential in the context of the EU Carbon Border Adjustment Mechanism (CBAM), which from 2026 will require importers of carbon-intensive goods such as steel, cement, aluminum, fertilizers and electricity to pay the difference between EU and domestic carbon prices. As a result, the existing UK–EU ETS price differential is increasingly translated into an effective cost wedge on UK exports to the EU, rather than remaining a purely domestic compliance gap. As free allocation in the EU ETS is phased out through 2034, this transmission of carbon price differences into border-adjusted costs is set to strengthen further. Taken together, ETS divergence and CBAM therefore increasingly embed carbon price differentials into trade frictions for energy-intensive UK exports to the EU.

Figure 9: Co-development of UK and EU ETS allowance prices (in EUR/tCO2)



Sources: LSEG Workspace, Allianz Research

UK economic and energy policies in need of a revamp

A decade after the Brexit referendum, the UK economy remains constrained by a few, but big, structural growth drags: elevated electricity costs and infrastructure bottlenecks. At the same time, the UK continues to boast many strengths. Productivity growth has been among the weakest in the developed world since the GFC, business investment remains low relative to peer economies, housing supply is chronically insufficient and infrastructure bottlenecks continue to constrain economic activity. Table 1 looks at the performance of the UK on key structural metrics relative to "well performing" developed economies which display elevated levels of income per capita: the US, the Netherlands, Denmark and Sweden. In terms of "output", the UK is clearly lagging behind in terms of productivity, but hours worked per working person and the employment rate are not particularly low, although the latter has improved less than peers since Brexit. In terms of education proficiency, the UK boasts good scores, particularly in science, and has even improved in country rankings in mathematics and reading proficiency. The UK devotes the largest budget to education (6.1% GDP). In terms of business environment and financial markets integration, the UK also scores well. High electricity costs and a low AI infrastructure index are where the UK really stands out as lagging behind.

In this regard, the current Labour government has correctly identified the economy's core challenges. Its emphasis on raising public and private investment and accelerating infrastructure delivery reflect a recognition that the UK's growth problem is fundamentally a supply-side problem. The government's reform agenda has also correctly highlighted the role played by excessive planning restrictions and regulatory barriers. According to the OECD, the UK's planning system imposes unusually high costs and uncertainty on investment projects. Lengthy and unpredictable permitting processes have become an important constraint on housing construction, infrastructure deployment and private investment, contributing to the country's weak capital accumulation and productivity performance. The consequences are visible in persistently high housing costs, lengthy approval processes and chronic underinvestment in transport, energy and industrial projects. The government's efforts to streamline planning procedures therefore target one of the most important barriers to long-term growth.

Similarly, the government's attempts to provide greater strategic direction and higher funding to industrial policy goes into the right direction. The Industrial Strategy identifies priority sectors – including advanced manufacturing, clean energy, defense, digital technologies and life sciences – in which the UK enjoys strong comparative advantages. The creation of the National Wealth Fund and additional support for clean-energy investment represent useful steps towards mobilizing private capital. Recently, the step-up of public funding toward AI hardware companies (GBP1.1bn) represents a welcome development.

Efforts to improve pay and working conditions in essential public services, particularly the NHS, are sound policies to be pursued. The government has well recognized that persistent recruitment and retention difficulties have weighed on labor participation, healthcare outcomes and overall economic performance. Restoring the attractiveness of these occupations is a necessary condition for improving public service delivery and raising the economy's productive capacity.

Table 1: Economic outcomes and performance of UK economy versus peers and change since Brexit

	Output			Education and Labour				Business		Innovation and AI						Energy	
	Productivity per hour	Hours worked per worker	Employment Rate	PISA Maths Scores Rank	PISA Reading Scores Rank	PISA Science Scores Rank	Educational Institutions Spending (% GDP)	Financial Markets Depth Index	Product Market Regulation	R&D (%GDP)	AI R&D (%GDP)	Total AI investment (% GDP)	AI R&D Index Rank (per capita)	AI Infrastructure Index Rank (per capita)	AI Investment Index Rank (per capita)	Electricity Cost ($ per KWh)	Wholesale Electricy Prices (€/Mwhe) - Average last 5 years
UK	74,0	1512	74,8	14	13	15	6,1	0,99	0,9	2,7	0,2	0,9	13	27	10	0,4	128,2
US	84,1	1796	71,9	34	9	16	5,8	0,99	1,6	3,5	0,4	1,2	5	7	2	0,2	
Denmark	92,3	1379	77,2	13	15	20	5,3	0,61	1,1	3,1	0,3	1,0	15	12	9	0,4	107,4
Netherlands	82,1	1445	82,3	10	35	25	5,0	0,96	0,9	2,3	0,2	1,5	16	9	13	0,3	117,5
Sweden	81,9	1431	76,7	22	18	21	5,3	0,93	0,8	3,6	0,3	0,8	12	5	3	0,2	66,1
Change since 2015	%	%	%	2018 Rank			GDP p.p.			GDP p.p.						%change since 2015-2019	
UK	5,0	-0,1	1,9	27	22	15	-0,1			0,4						135,5	
US	14,9	-1,9	4,6	40	24	25	-0,3			0,7							
Denmark	8,5	-2,0	6,8	12	18	21				0,0						223,2	
Netherlands	0,5	-0,3	8,7	11	15	17	-0,4			0,1						186,1	
Sweden	5,0	-2,4	1,6	24	17	28	0,0			0,4						99,0	

Sources: various, Allianz Research

Restoring the attractiveness of these occupations is a necessary condition for improving public service delivery and raising the economy's productive capacity.

However, while the government's diagnosis is broadly correct, implementation has often fallen short of its ambitions. Despite the government's emphasis on industrial policy, funding commitments remain modest relative to the scale of the challenge. Public support for strategic sectors remains fragmented across numerous programs and falls short of the large-scale industrial policies pursued by competitors such as the US, China and increasingly the EU. The result is a mismatch between ambitious rhetoric and limited fiscal resources. Similarly, some of the initial ambition of planning reform has been diluted in response to political opposition, raising concerns that housing supply and infrastructure delivery may not improve sufficiently to alter the UK's long-term growth trajectory.

Questions also arise regarding the credibility of the fiscal strategy. The increase in employer National Insurance (NI) Contributions in 2025 raises the cost of labor at a time when the economy requires stronger hiring, investment and labor demand. From an efficiency perspective, greater reliance on broad-based consumption taxes such as VAT would likely have generated similar revenues while imposing fewer distortions on employment decisions. The government has also relied heavily on relatively narrow tax measures targeting capital gains, carried interest and non-domiciled taxpayers, despite the fact that such revenue sources are often uncertain and susceptible to behavioral responses. Table 2 depicts the key public expenditures and revenues ratios for the UK against the "well performing" peer countries. Figures from the OECD (for cross-country comparisons purposes) are only from 2024, but highlight that the UK has a relatively low tax take on goods & services consumption (essentially VAT), and this take has decreased since Brexit (at 10.2% GDP vs over 11% in Sweden and Denmark). VAT is one of the least distortive form of taxation (ie with limited negative effect on potential growth[6]). Social security contributions, while starting from a relatively low level, have increased, and the NI contributions hike in 2025 would have increased the ratio further. Meanwhile, a substantial share of the planned fiscal consolidation is backloaded towards the latter years of the Parliament. This reduces confidence that the measures will ultimately be implemented. Markets typically discount future fiscal tightening when political incentives may change before implementation occurs. This contributes to uncertainty regarding the medium-term fiscal outlook and may increase the risk premium demanded by investors, leading eventually to higher funding costs for the private sector, weighing on business investment – a key constraint on growth.

6 VAT has several appeals over some other forms of taxation: it does not directly discourage work, it is difficult to avoid, it raises a lot revenue

Table 2: Selected public expenditures & revenues ratios

	Fiscal Policy				Healthcare and Social Spending		
	Firms' Income, Profits and Capital Gains Tax	Goods and Services Taxes	Social Security Contributions (% GDP)	Personal Income and Capital Gains Taxes (% GDP)	Healthcare Spending (% GDP)	Public social expenditure (% GDP)	Public expenditure on pensions (% GDP)
UK	3,5	10,2	6,1	10,8	11,1	23,0	7,1
US	2,2	4,1	6,0	10,3	17,2	19,8	7,3
DK	4,2	12,3	0,1	25,2	9,4	26,4	7,5
NL	4,3	11,1	12,0	9,8	10,0	18,9	6,4
SW	3,9	11,2	9,0	11,3	11,3	26,1	8,0
Change since 2015	GDP p.p.	GDP p.p.	GDP p.p.	GDP p.p.	GDP p.p.	GDP p.p.	GDP p.p.
UK	1,19	-0,71	0,11	1,96	1,2	-3,7	-1,2
US	0,14	-0,20	-0,17	-0,23	0,8	0,3	0,4
DK	1,15	-2,23	-0,02	-0,07	-1	-1,3	-0,4
NL	1,63	-0,05	-1,74	2,33	-0,2	-0,7	-0,1
SW	0,93	-0,98	-0,61	-1,33	0,4	1,3	-0,3

Sources: OECD, Allianz Research

A durable growth strategy requires a fundamental overhaul of the UK's fiscal rules and fiscal framework. On top of poor fiscal policy choices, credibility is also undermined by poorly designed fiscal rules — a subject often overlooked. The current fiscal framework relies on two principal fiscal rules: public sector net debt must be falling as a share of GDP in the fifth year of the forecast horizon, while the current budget must be in balance over the same period. These targets are problematic because both depend heavily on forecasts produced by the Office for Budget Responsibility (OBR) and are assessed at a moving five-year horizon. As a result, governments can often satisfy the rules through relatively small forecast revisions rather than genuine improvements in underlying fiscal sustainability. The framework is therefore complex, opaque and poorly understood outside specialist circles. A simpler framework combining a medium-term expenditure growth rule with a deficit ceiling would offer substantial advantages. Spending rules are transparent, easier to monitor and less vulnerable to forecast manipulation. They also allow automatic stabilizers to operate during downturns, thereby supporting macroeconomic stabilization without requiring repeated discretionary interventions. Such frameworks have generally delivered stronger fiscal discipline and greater credibility in several northern European economies.

Reducing deficits and creating additional fiscal space will require confronting the rapid growth of age-related spending. Although UK public pension spending remains moderate by international standards (at around 7% GDP, see Table 2), the triple lock creates a source of spending growth that is difficult to justify in the context of mounting demographic pressures. By guaranteeing annual increases based on the highest of inflation, earnings growth or 2.5%, the mechanism tends to raise pension incomes faster than required to preserve either purchasing power or relative living standards. As the population ages, this implies a steadily rising claim on public resources. Reforming the triple lock would therefore not address an immediate pension crisis, but rather prevent future spending pressures from crowding out public investment in areas such as housing, infrastructure, innovation and healthcare that are more likely to support long-term growth.

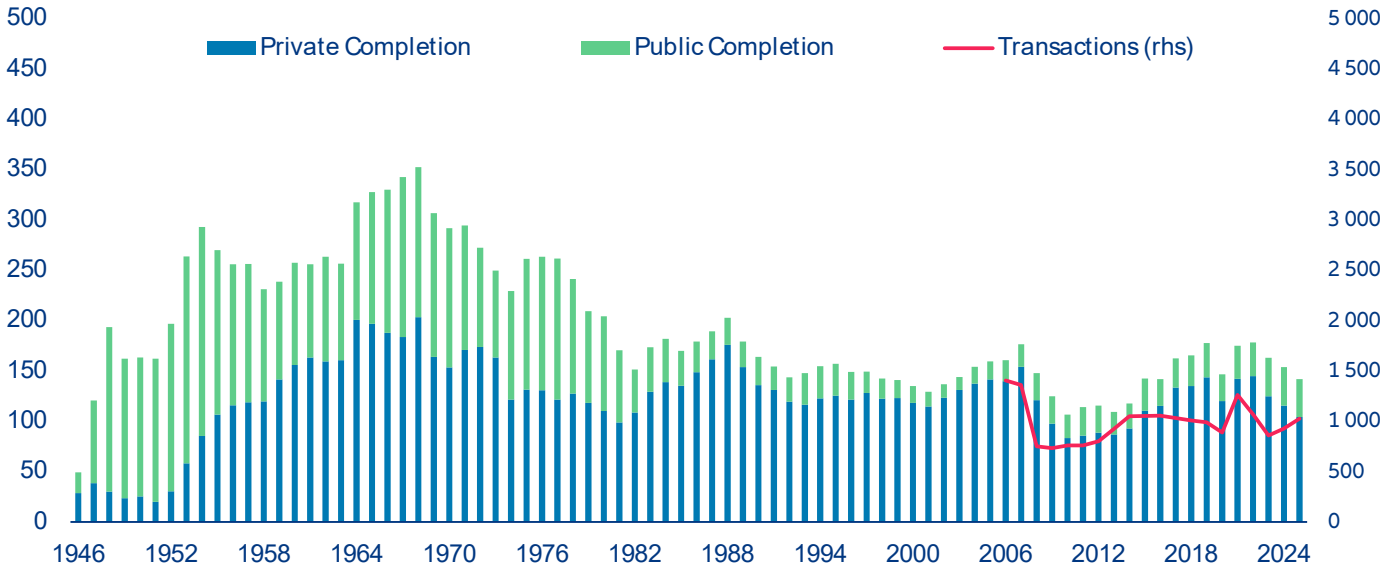
Fiscal consolidation should rely on a more efficient tax mix. A broader VAT base (reduced exemptions and zero rates), continued fiscal drag through temporarily frozen income-tax thresholds and reform of the pension triple lock would raise significant revenues while imposing relatively limited costs on growth. Part of the proceeds could be directed towards lower-income households. At the same time, the government should eliminate distortions within the tax system, notably the effective 60% marginal tax rate faced by individuals earning between GBP100 000 and GBP125 000. Additional savings could be generated through improvements in public-sector productivity, procurement reform and greater administrative efficiency. The government should consider reforming property taxation, which remains based on decades-old valuations and imposes fewer distortions on growth than taxes on labor or business investment[7]. The resulting fiscal space could be directed toward defense, housing, infrastructure, healthcare and innovation, strengthening both the sustainability of the public finances and the economy's long-term growth potential.

Doubling down on housing policy and the NHS should occupy a central place in the government's growth strategy. While planning reform is essential, it is unlikely on its own to generate the scale of construction required to close decades of underbuilding. The public sector therefore has an important role to play both through direct investment and by supporting local authorities and housing associations. From 1950 to1970, the building of public housing was behind the surge in housing construction, while the private sector's role never really took off. Increasing housing supply would generate benefits extending far beyond the construction sector. Lower housing costs would raise real disposable incomes, reduce welfare expenditures linked to housing support and improve labor mobility by allowing workers to relocate more easily to areas with stronger employment opportunities. More affordable housing would also reduce cost pressures on employers and improve the allocation of labor across the economy. Meanwhile, addressing the NHS' core challenges should be a top priority, rather than focusing on cutting disability benefits, where the current government faced stiff opposition from backbench Labour MPs on its welfare reform. The government's objective should not simply be to reduce benefit expenditure, but to address the underlying drivers of inactivity through improved healthcare provision, faster treatment, stronger occupational health support and more effective incentives to remain connected to the labor market. Long waiting times for treatment delay the return of workers to employment, increase absenteeism and weaken productivity. Improving healthcare capacity, investing in preventative care and addressing workforce shortages within the NHS would therefore yield economic returns beyond the healthcare sector itself. A healthier workforce is more productive, participates more actively in the labor market and imposes lower fiscal costs on the state. In an ageing society facing persistent labor shortages, improving population health may represent one of the most effective ways of expanding the economy's productive capacity.

One often overlooked feature of the UK's productivity problem is that it does not primarily stem from a lack of innovation. The UK hosts world-class universities, a vibrant start-up ecosystem and globally competitive firms in sectors such as finance, life sciences and artificial intelligence. Rather, the challenge lies in the diffusion of innovation across the wider economy. OECD research shows that productivity growth at frontier firms has remained robust, while the gap between leading and lagging firms has widened over time. In the UK, a relatively small number of highly productive firms and regions have continued to innovate, but many smaller firms have struggled to adopt new technologies, invest in digitalization and upgrade workforce skills. As a result, the benefits of innovation have not spread sufficiently across sectors and regions. Improving technology diffusion through stronger investment incentives, skills policies, business support programs and closer collaboration between universities and firms could therefore represent one of the most effective ways to raise economy-wide productivity growth

7 The UK's main recurrent residential property tax, Council Tax, is still based on property values assessed in England in 1991 (2003 in Wales). As a result: a £500,000 property and a £5 million property may face similar tax bills, effective tax rates fall as property values rise. The system is therefore regressive with respect to property wealth. Moreover, the UK taxes transactions heavily instead of ownership.

Figure 9: Housing completions & housing transactions (000s per year)



Sources: LSEG Workspace, Capital Economics, Allianz Research

On energy policy, the Brexit-related energy costs point to three priorities, two of which are already the subject of active negotiations. The most immediate is completing IEM reintegration: the post-Brexit shift to explicit capacity auctions has contributed to a persistent UK wholesale price premium over continental markets, with efficiency losses that grow as electricity import dependence increases. Following the May 2025 Lancaster House Summit, the EU Council authorized the Commission in March 2026 to open negotiations on UK participation in the Internal Electricity Market. These talks are time-sensitive: delays prolong consumer costs and investment uncertainty around interconnector capacity, while the potential efficiency gains remain material at system scale.

A second priority is linking the UK and EU ETS. The UK carbon price discount has evolved from a domestic pricing divergence into a direct trade cost via CBAM for energy-intensive exports, an effect that strengthens as EU free allocation is phased out through 2034. The May 2025 summit established a political agreement in principle to pursue linkage, with CBAM exemption forming the central commercial rationale. Translating this into a binding agreement is the most direct near-term lever to limit carbon-related trade frictions.

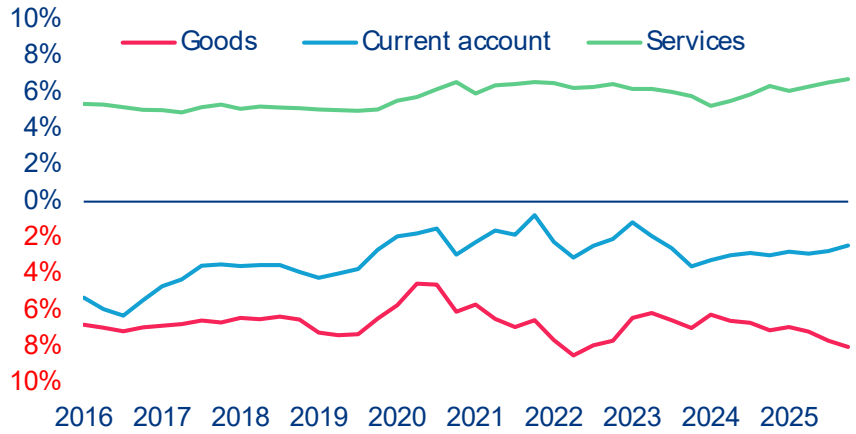
The third focus should lie on deepening North Sea infrastructure cooperation. The "Great Grid Upgrade" remains essential to address the UK's internal north–south transmission bottleneck by connecting Scottish renewable generation to demand centers in the south. In parallel, deeper coordination under the North Seas Energy Cooperation framework offers scope to reduce system costs through shared offshore grid planning and hybrid interconnector development, particularly in the southern North Sea where congestion pressures and offshore wind expansion most directly overlap. While these initiatives would not substitute for domestic grid investment, they can partially ease balancing constraints and improve cross-border optimization in an increasingly interconnected regional system.

The UK's productivity challenge ultimately requires a broader investment strategy. Energy costs remain significantly higher than in many competing economies, reducing the attractiveness of the UK as a destination for manufacturing and capital-intensive investment. Accelerating grid expansion, nuclear deployment and domestic energy production should therefore be viewed as industrial policy as much as energy policy. At the same time, the UK should expand support for innovation through a combination of enhanced R&D tax incentives and mission-oriented public investment. While institutions such as ARIA, Innovate UK and the National Wealth Fund move in this direction, they remain considerably smaller than programs such as France 2030 or the industrial initiatives introduced under the US Inflation Reduction Act and CHIPS Act. A more ambitious innovation strategy, combined with housing and infrastructure investment, would help address the UK's longstanding productivity shortfall and strengthen the economy's capacity to generate sustainable growth in the post-Brexit era.

The UK's trade performance: goods imports substitution, services trade powering ahead

The UK's goods trade deficit has worsened since Brexit but rising services surplus have offset this rise. The UK's trade deficit in goods increased by +1.3pp of GDP (and by +1.5pp incl. gold) between 2016 and 2025, rising from 6.7% of GDP to 8.0% of GDP (Figure 10). The UK runs a goods trade deficit with most of its major trading partners. Around one-third of the total deficit is attributable to trade with the EU-27 (USD110bn), which represents a decline compared with 2016, when 70% of the deficit came from the EU-27). Commonwealth countries account for 8% of the deficit (22% incl. Gold), while China accounts for 28% and the US 7%. On services, the UK's substantial surplus helps offset much this widening goods trade deficit. As a result, the current account balance has remained relatively stable over time and has even shown a modest improvement, reaching a deficit of USD97bn (2.4% GDP) by the end of 2025. This highlights the continuing importance of the UK's services sector – particularly financial, professional and business services – in mitigating the deterioration of its goods trade balance.

Figure 10: UK current account balance breakdown (four-quarter moving sum, % GDP)

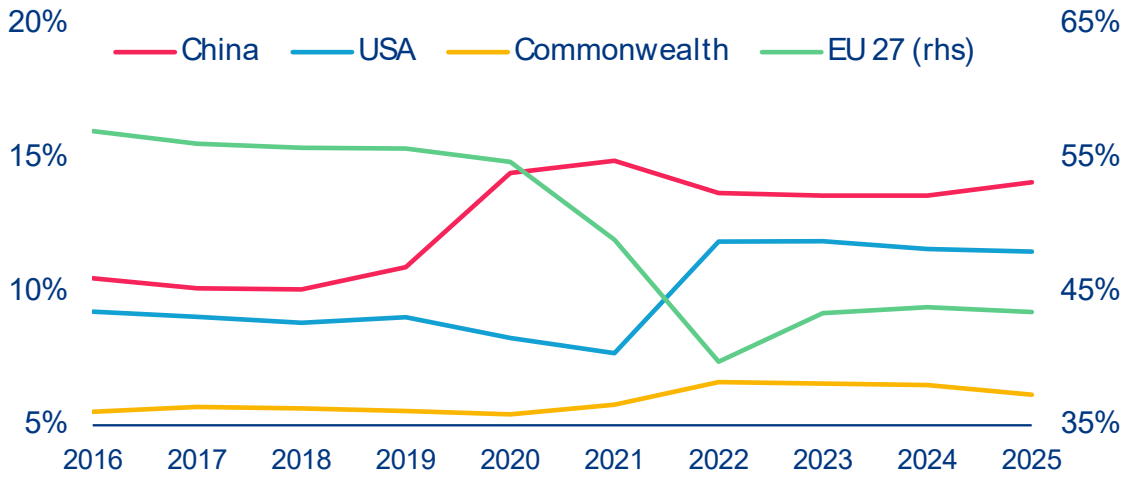


Sources: IMF BoP, Allianz research

Since the Brexit vote in 2016, the structure of UK goods exports toward foreign partners has not changed much. However, on the import side, major economic blocs have benefited from the reorientation of UK trade away from the EU. UK goods exports have decreased by 2.9pp of GDP since the Brexit vote, reaching 11.2% of GDP in 2025. The EU remains the UK's largest export market, accounting for 48% of total goods exports, a share that has remained stable from 50% in 2016. The shares of other major partners such as the US, the Commonwealth countries and China have also remained relatively stable. On the import side, however, changes have been much more significant. Total imports increased by 2pps of GDP between 2016 and 2025, reaching 18.7% of GDP. At the same time, the composition of imports has shifted substantially (Figure 11). The EU now accounts for 43% of the UK's total goods imports, compared with 57% a decade ago. Meanwhile, the importance of China and the US has grown, representing 14% (vs 10%) and 11% (vs 9%), of total imports, respectively. Two main factors explain these developments: First, imports from China surged since the pandemic, driven by strong demand for technology goods, and second, imports from the US increased significantly following the outbreak of the war in Ukraine, largely due to energy purchases.

The UK has diversified both its sources of supply and the types of goods it imports, notably through increased reliance on Chinese manufactured goods and US energy exports. Today, UK imports are dominated by machinery, chemicals, agrifood and automotive products. Compared with 2016, the composition of total imports across these products has become more balanced. Energy imports also gained importance, while chemicals, textiles, transport equipment and automotive products experienced a decline in their relative shares of total imports. A closer look at the changing composition of the UK's suppliers reveals substantial shifts between 2016 and 2025. China has made the most significant gains, particularly in electronics and electrical equipment (the UK is the top destination, with 35% total gross imports of this category), a trend similar to that observed in the EU's growing dependence on Chinese technology goods. China has also increased its presence in automotive products, machinery, chemicals and transport equipment. In short, it has expanded its market share across virtually all manufacturing sectors. Meanwhile, the US has strengthened its position in energy imports, increasing its share by 16pps of the UK's total energy imports. It has also gained ground in machinery and chemicals. Finally, Commonwealth countries have expanded their presence across nearly all sectors, particularly in textiles and chemicals, but the overall share is stable (+0.6pp).

Figure 11: Share of global gross goods imports of the UK by main partner (excluding gold)

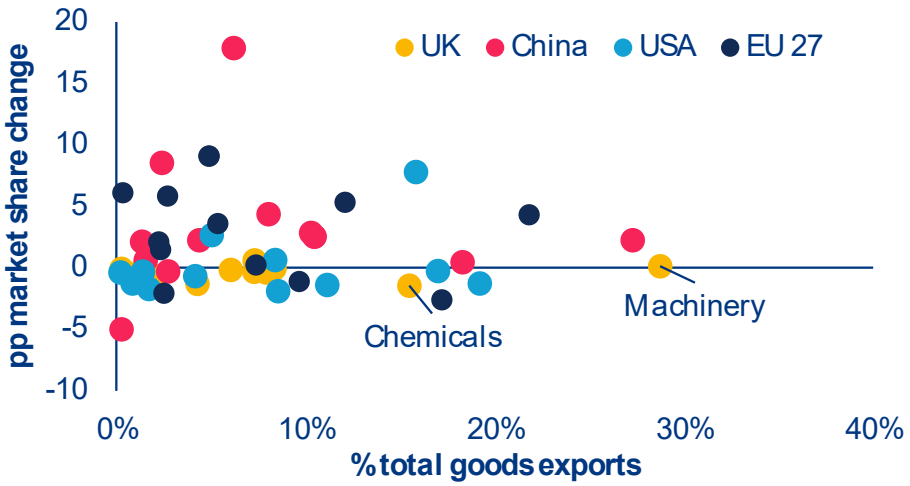


Sources: Trade Map, Allianz research

UK exports have reduced their market shares. Exports are more concentrated in machinery, with a loss of market shares in some traditional strengths (autos, chemicals). Machinery exports are primarily composed of turbojets, turbopropellers, other gas turbines used in the aerospace industry and specialized medical equipment. They now account for almost 30% of total gross exports. By contrast, the importance of the automotive and chemicals sectors has declined significantly. The share of chemicals in total goods exports fell from 20% to 15%, while the automotive sector's share decreased from 13% to 9%, a trend also reflected in broader transport equipment exports. These declines are visible not only in relative terms but also in absolute values, with automotive exports falling by 20% and chemical exports by 8% between 2016 and 2025. At the product level, the UK exports less to the EU across most products than it did in 2016 (as a share of total gross exports), with the notable exceptions of transport equipment and energy. However, these declines have not been offset by a another economic bloc in relative share. Although the UK's export structure appears relatively stable in relative terms, with the same trading partners and some rebalancing across products, this masks significant shift towards machinery and energy exports, alongside a decline in sectors that have traditionally been among the UK's strengths, namely automotive and chemicals. Figure 12 shows that overall, the UK has experienced a decline in its global market share across most of the products it exports compared to the other major economic blocks.

This analysis of UK trade excludes gold exports and imports, a category in which the UK has experienced strong growth in market share and which has had a significant impact on its trade structure as a result of the gold price rally in recent years. Including gold could distort the assessment of the underlying state of British manufacturing capabilities and the structural shifts currently taking place in global trade, such as the growing footprint of Asian economies — particularly China — across most goods categories, and the increasing role of the US in energy supply. When gold is included, the UK's degree of openness remains broadly unchanged at around 38% between 2016 and 2025. Excluding gold, however, the indicator points to a weakening integration of UK into global trades, with a share that decreased from 35% in 2016 to 30% in 2025.

Figure 12: Market share changes 2025 vs 2016 (vertical axis) and share of total gross exports of the country by product in 2025

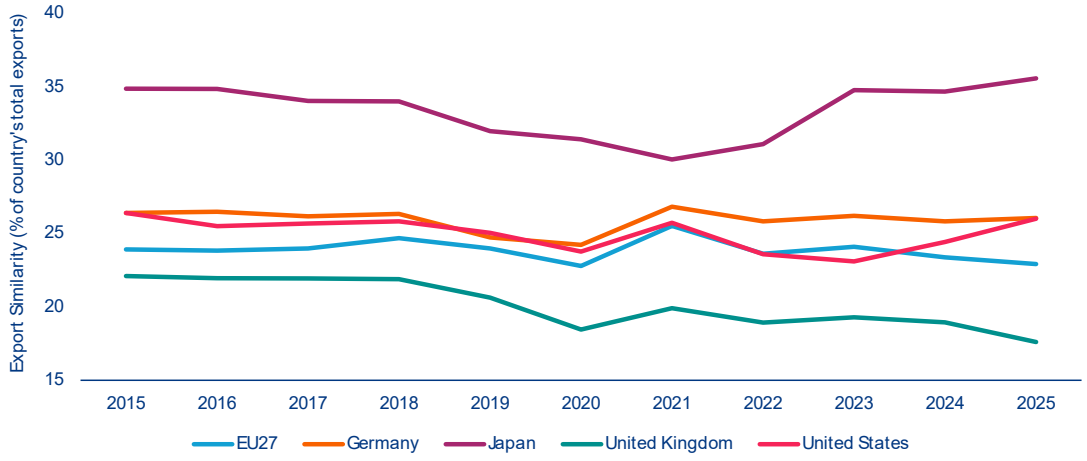


Sources: Trade Map (H2 classification), Allianz research

With regard to Chinese competition, the UK is less exposed. In 2025, about 15% of UK exports were in products among the top 25 of China's exports . In contrast, 25% of US exports and 26% of German exports compete directly with the Asian giant's top exports. As China has moved towards high-value manufacturing, its top exports now consist of telecommunication devices, integrated circuits and computers. The UK, historically a smaller exporter of electronics, is thus less exposed to Beijing's shift. Pharmaceuticals and aerospace, a large source of the UK's competitiveness advantage, are less in the crosshairs. Since the pandemic, a key area of competition is also the automobile industry. Cars represent the UK's second largest source of exports at over USD30bn per year. A falling similarity index could be a cause for concern. Indeed, a lack of competitiveness that erodes a sector's share in total exports will mechanically decrease the index. For the UK, car exports have increased by +1.1% in nominal value since 2022 while total exports (excl. gold) increased by +11.2%, highlighting a flailing automotive sector and thus decreasing the similarity index.

UK trade agreements have expanded market access, but they have not matched the scale of the economic relationship with the EU or fully offset Brexit-related trade losses. Although UK–EU tariffs remain relatively low, with an average applied tariff of 1.5% (reaching up to 19% for certain products), the principal barriers to trade are non-tariff measures (NTMs). Since leaving the EU in 2020, the UK has introduced 58 trade-related measures affecting EU countries, including 25 export-related measures, 20 subsidies, seven tariff measures and five price controls. Over the same period, the EU has introduced 337 measures affecting the UK, predominantly subsidies (275), alongside export restrictions (19), tariff measures (15), licensing and quota measures (13), price controls (six), trade-protective measures (four) and one foreign direct investment (FDI) measure. These policy changes have contributed to a significant decline in bilateral trade integration. Structural gravity estimates suggest that Brexit reduced UK–EU trade by -21.3% for goods and -49.7% for services. This weaker bilateral performance reflects Brexit-related trade and supply-chain disruptions arising primarily from higher NTMs and, to a lesser extent, tariffs.

Figure 13: Similarity index to Chinese goods exports



Sources: ITC Trade Map, GTA, Allianz Research

Note: Using GTA methodology, similarity is calculated for each country as the sum of the export value of all their products appearing in China's top 25 HS4 codes, divided by their total exports. The HS code for cars is included for all years.

7 The UK's main recurrent residential property tax, Council Tax, is still based on property values assessed in England in 1991 (2003 in Wales). As a result: a £500,000 property and a £5 million property may face similar tax bills, effective tax rates fall as property values rise. The system is therefore regressive with respect to property wealth. Moreover, the UK taxes transactions heavily instead of ownership.

In parallel, the UK sought to offset some of the economic costs of Brexit through an independent trade policy. Since Brexit, the UK's free trade agreement (FTA) strategy has evolved from initially rolling over agreements previously negotiated through EU membership to pursuing new bilateral and plurilateral arrangements. Major milestones include agreements with Japan (2020), Australia (2021), New Zealand (2022), the EEA EFTA states (Norway, Iceland and Liechtenstein), digital trade agreements with Singapore and Ukraine, accession to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in 2024, the India FTA signed in 2025, an upgraded agreement with South Korea and the Gulf Co-operation Council (GCC) agreement concluded in 2026 but not yet in force (Table 3). Collectively, these post-Brexit agreements account for approximately 21% of UK trade in 2025 (without the US, which is a prosperity deal to offset the impact of imposed tariffs rather than a FTA). The UK is also negotiating or upgrading agreements with Canada, Switzerland and Türkiye. Despite expanding the UK's global trade network, the scale of these agreements remains substantially smaller than the UK's economic relationship with the EU, which continues to account for the largest share of UK trade at 37% in 2025.

Deeper UK–EU trade ties could unlock billions in economic gains. Looking ahead, the UK and EU may find scope for greater alignment in goods trade, while the UK and US are more likely to deepen cooperation in services, technology, finance and regulation. However, only a limited share of the trade frictions created by Brexit is likely to be reversed. Computable general equilibrium (CGE) simulations indicate that a deep UK–EU trade agreement could generate annual gains of USD25.2bn for the UK, comprising USD19.6bn in trade creation and USD5.6bn in trade diversion. This would increase the value of UK exports to the EU by +23.1%, with the largest proportional gains in sugars, food preparations and cereals, followed by vehicles, alcoholic beverages and textiles. EU countries could gain USD31.9bn annually (+17.4%), driven primarily by vehicles — reflecting the restoration of previously integrated value chains — as well as food preparations, dairy products and chocolate.

Table 3: UK Free Trade Agreements since Brexit

Partner	Agreement	Year	Key provisions	UK bilateral trade (share of total UK trade in 2025)
European Union	EU–UK Trade and Cooperation Agreement	2020 (effective 2021)	Necessary replacement for EU membership. Zero tariffs and quotas on qualifying goods, customs cooperation, services framework, fisheries, transport, energy, law-enforcement cooperation	37% with EU remaining the UK's largest trade partner
Japan	UK–Japan CEPA	2020	Goods market access, digital trade, financial services, data flows, investment protections.	1,50%
Australia	UK–Australia FTA	2021 (effective 2023)	Tariff elimination, services access, mobility provisions, digital trade, procurement.	1,30%
New Zealand	UK–New Zealand FTA	2022 (effective 2023)	Near-total tariff elimination, services liberalization, digital trade, investment access.	0,10%
Norway, Iceland, Liechtenstein	UK–EEA EFTA FTA	2021	Goods, services, investment, digital trade and mobility provisions.	2,30%
Singapore	Digital Trade Agreement	2022	Digital identities, e-commerce, fintech cooperation, cross-border data flows.	1,00%
Ukraine	Digital Trade Agreement	2023	Digital trade rules, e-signatures, cybersecurity cooperation, data flows.	0,20%
Comprehensive and Progressive Agreement for Trans-Pacific Partnership	UK accession to CPTPP	2023 (effective 2024)	Tariffs, services, investment, procurement, digital trade across 11 Pacific economies.	9,20%
India	UK–India FTA	2025 (not yet in force)	Tariff reductions, services access, professional mobility, customs simplification, investment provisions. Expected to increase bilateral trade substantially.	1,70%
South Korea	UK-South Korea FTA	2025 (updated from earlier EU agreement)	Replaces the continuity agreement inherited from EU membership. Modernizes rules of origin, services and digital trade, maintains tariff-free access on most goods, and strengthens access for automotive, financial services and technology sectors.	0,90%
United States*	Economic Prosperity Deal	2025 (partially implemented)	A non-binding framework intended to reduce the impact of US tariffs and improve market access. Includes preferential treatment for UK autos, aerospace, steel and aluminum, and a framework for future cooperation on pharmaceuticals and supply-chain security.	13,40%
Gulf Co-operation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE)	UK-GCC FTA	2026 (not yet in force)	The UK's first FTA with the GCC and the GCC's first FTA with a G7 country. Covers tariff reductions, customs facilitation, services, investment and market access.	2,60%

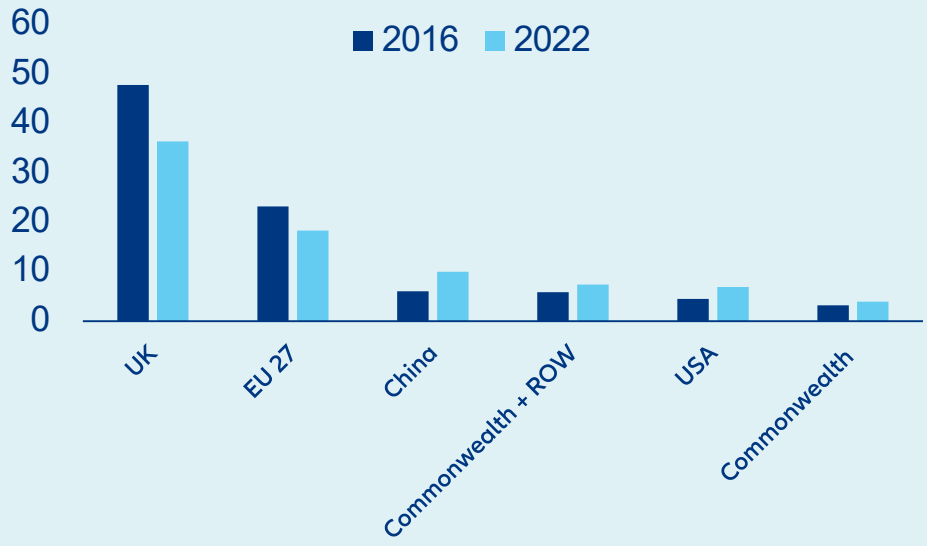
Sources: UNComtrade, UK House of Commons, Allianz Research. Notes: *The US Economic Prosperity Deal is not a FTA, but a deal to lower the impact of tariffs

The evolution of UK trade in global supply chains

From a supply-chain perspective, the UK's domestic demand has become increasingly dependent on industrial foreign suppliers' inputs, while the country has struggled to expand its export footprint in global supply chains. The OECD Trade in Value Added (TiVA) dataset has data only available up to 2022, yet it provides valuable insights into the changes to supply-chains. It looks at the foreign and domestic value added embodied in final demand. For the UK, the data indicates a gradual reorientation of domestic demand away from EU products. Although the EU remains the UK's largest trading partner in valued added, the older EU member states are no longer its preferred trading counterparts in supply chains as the relative importance of partners such as China, the US and Commonwealth countries has increased significantly over the past decade.

Indeed, between 2016 and 2022, the share of industrial foreign value added in UK final demand originating from the EU declined from 52% to 39% in the manufacturing sector. Over the same period, China's share increased by 8pps, making it the UK's largest single-country partner in 2022. The US gained 2pps and became the second-largest partner, while Germany's share fell by 8pps, causing it to drop from first to third place. Within the EU, only Ireland and Poland increased their shares, whereas most Western European countries experienced a decline. This shift is particularly pronounced in the computer, electronics, and optical products sector, where China's share has overtaken that of the EU. Similarly, in the motor vehicles industry, the US gained around 5pps, again at the expense of both EU and UK manufacturing value added. These trends suggest a gradual reconfiguration of the UK's supply chains away from its historical European partners and towards a more globally diversified network of suppliers. In terms of UK exports, between 2016 and 2022, the UK has lost a bit of market share in the trade in value added embodied in other countries' final demand for manufacturing (-0.4pp at 1.6% at the global level), visible for the main UK's industries (chemicals, electronics, machinery, automotive) .

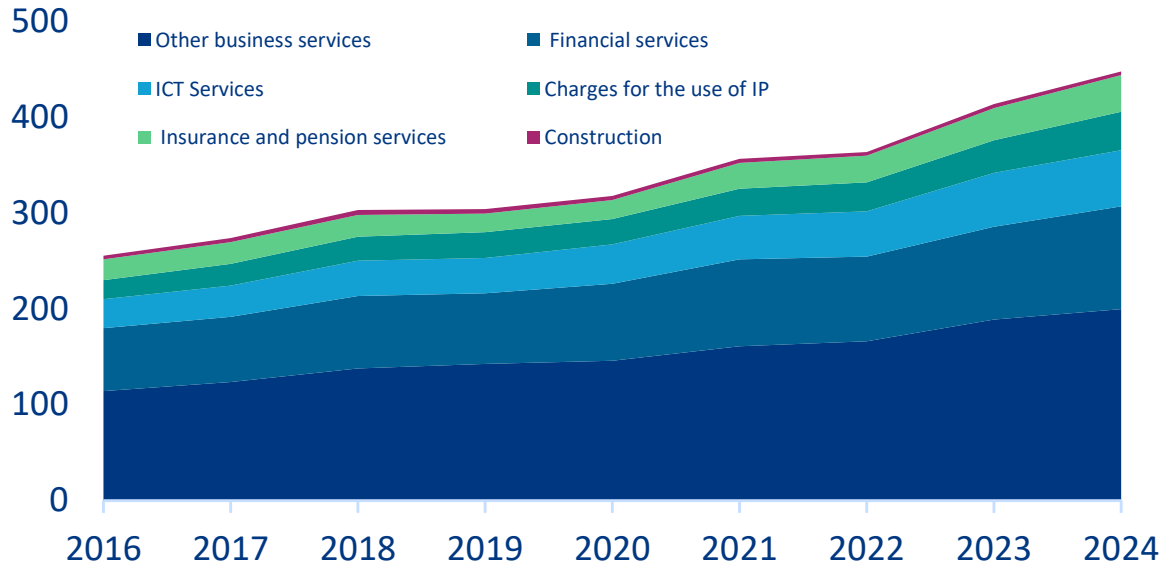
Figure 14: Insurance penetration, selected countries (gross written premiums in percent of GDP)



Source: OECD TiVA, Allianz research

While Brexit introduced additional compliance requirements and regulatory uncertainty, the services sector has largely avoided the trade frictions experienced in goods markets. UK services exports to the EU increased by USD96bn between 2026 and 2024, representing growth of +63%, only slightly below the pace of growth in UK services exports globally (+65%). Financial services have retained much of their international competitiveness despite the loss of preferential access to EU markets. While some trading activity, assets and jobs shifted to Amsterdam, Dublin and Paris, London remains Europe's leading center for foreign exchange, derivatives, insurance and international banking. Financial services exports to the EU grew by 58% between 2026 and 2024, compared with 63% globally. Moreover, while the UK's share of value added embodied in global final demand for financial services decreased by 0.3 percentage points between 2016 and 2022, its share in EU-27 final demand increased by 0.6 percentage points, suggesting a deeper integration of the UK financial sector into European value chains. The share of financial services in total UK service exports has remained broadly stable at around 17% in 2024[9] . The UK's trade surplus in financial services has increased over the period and the export destinations remain heavily concentrated in the US, which accounts for around 27% of UK financial services exports, followed by Ireland, Luxembourg, other EU member states and a range of offshore financial centers. In the global financial services market, the UK's position has remained remarkably resilient. It continues to rank second worldwide, accounting for approximately 21% of global financial services exports, outperforming the EU and behind the US, which retain the first place. The main changes in the global ranking have occurred among the following positions, with Singapore notably strengthening its role and consolidating its position as the fourth-largest exporter of financial services. These trends suggest that while Brexit has not significantly enhanced the UK's dominance in financial services, neither has it undermined London's status as one of the world's leading financial centers. Actually, the UK is exporting mostly "other business services" more than financial services + insurance and pension services, including "R&D services", "consulting services" and "technical, trade-related services" (Figure 15). Finally, ICT services have done even better. Supported by digital trade provisions in the EU–UK Trade and Cooperation Agreement and continued EU data adequacy arrangements, UK ICT services exports to the EU grew by +94% since Brexit, outpacing growth to the rest of the world (+76%).

Figure 15: Distribution of UK's services exports (USD Bn)



Sources : WTO-OECD, Allianz research

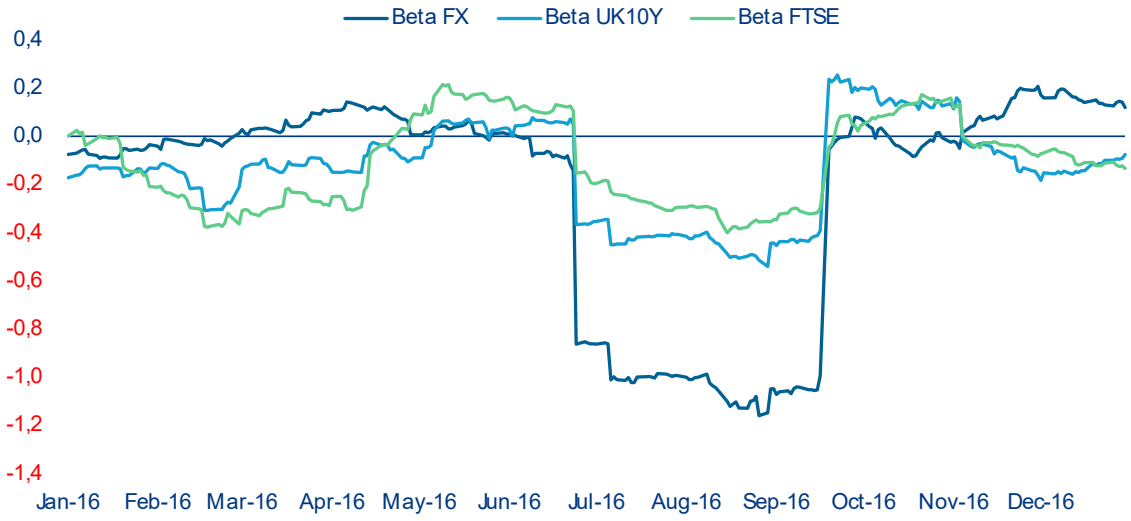
9 From a value-added perspective, financial service activities accounted for 4.4% of total UK value added in 2023, down from 6.5% in 2016

Financial markets: unofficial dollarization and eroding confidence but the City of London keeps (most of) its shine

From a capital market perspective, Brexit set in motion a sequence of structural changes — monetary, institutional and commercial — whose cumulative effects only became visible after the central bank's protective cover was removed.

The immediate market impact of the referendum was absorbed almost entirely by the exchange rate. From the moment Leave probabilities began rising in late 2015, sterling traded as the primary signal of UK political and growth uncertainty. The Gilt market was insulated: the Bank of England cut rates and relaunched asset purchases within weeks of the result, compressing term premia and anchoring the long end of the curve. The primary driver of Gilt yields throughout this period was the global rates cycle — Fed signaling above all — rather than any UK-specific risk premium. Quantitative easing masked the Brexit effect on rates; the FX market was the honest signal, the bond market the managed one. On the day the referendum result was announced, 24 June 2016, the GBP/USD fell ~8.1% in a single day — a 14.8-sigma move relative to its normal daily volatility, by far the most extreme reaction of any asset. By contrast, the UK 10Y yield moved -28.8bp (z = -5.3) and the US 10Y just -16bp (z = -3.1), while the FTSE 100 fell -3.1% (z = -3.3). In standardized terms the currency shock was roughly three to five times larger than the rates and equity shocks. The Gilt had, in effect, become a UST proxy at a discount, its terminal rate tracking US conditions more closely than domestic fundamentals.

Figure 16: Rolling 61-day beta (z-score returns) vs policy index – Zoom 2016, Brexit 24/06



Sources : LSEG Datastream, Allianz Research

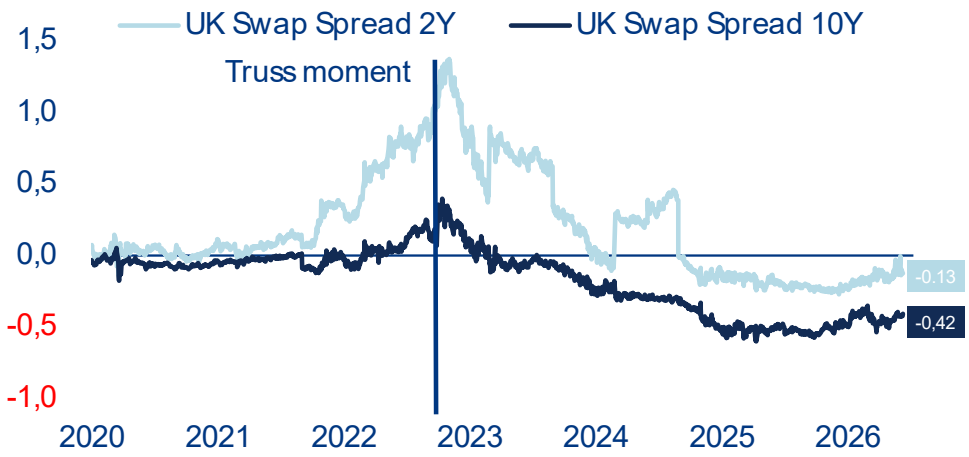
Beneath this surface stability, Brexit was accelerating a structural reorientation of the UK's external sector. The share of UK exports invoiced in GBP fell from approximately 63% before 2015 to 38% by 2022, with USD invoicing rising from one-third to 45% over the same period This transition was directly triggered by the currency-mismatch valuation shock of the 2016 depreciation and proved persistent. As the UK economy became progressively coupled with US financial conditions, the dependency on Fed policy transmission deepened. This dollarization of trade was the most consequential — and least visible — legacy of the referendum years. The risk premium currently visible in GILT was not observable right after Brexit.

The City's resilience post-Brexit has proved more robust than pre-referendum predictions suggested, but headline stability conceals a meaningful structural shift at the margin. London's pre-eminence was built on two foundations: its historical role as the birthplace of the Eurodollar system and its subsequent emergence as the natural bridge between dollar and euro financial markets. It hosted the clearing infrastructure for euro-denominated derivatives on LCH, the primary market for rates and FX instruments across both currencies and the center of international banking for non-domestic entities operating in Europe.

The aggregate BIS data tells a story of remarkable persistence. In April 2025, the UK accounted for 49.6% of global OTC interest rate derivatives turnover – up from 42.9% in 2022 – and handled 37.8% of global FX turnover, broadly stable versus the pre-Brexit baseline (BIS Triennial Survey, 2025). These figures point not only to an expansion in gross activity but also underline the UK's persistent global leadership. The depth of London's liquidity pool and the network externalities that make migration costly have proved more durable than political pressure alone could dismantle.

The euro clearing franchise is where nuance matters. LCH retained approximately 81% of global euro IRS clearing as of end-2023, with Eurex holding the remaining 19% – a shift that occurred almost entirely in the 2019–2021 window driven by Brexit uncertainty and Eurex incentive programs, and which has not materially progressed since (ECB Financial Integration Report, June 2024). Around 95% of euro-denominated interest rate swaps were still cleared through LCH in 2024, and the European Commission's renewal of UK CCP equivalence until June 2028 is a tacit acknowledgement that the infrastructure cannot be relocated by political fiat. The exception is euro repo, the one segment where migration has been documented and sustained: London's banking ties to the Eurozone have loosened in part owing to the shift of euro repo clearing from London to Paris (BIS Bulletin No. 65, 2022; ICMA repo survey data, 2024).

Figure 17: Swap spread widening after the Truss moment.



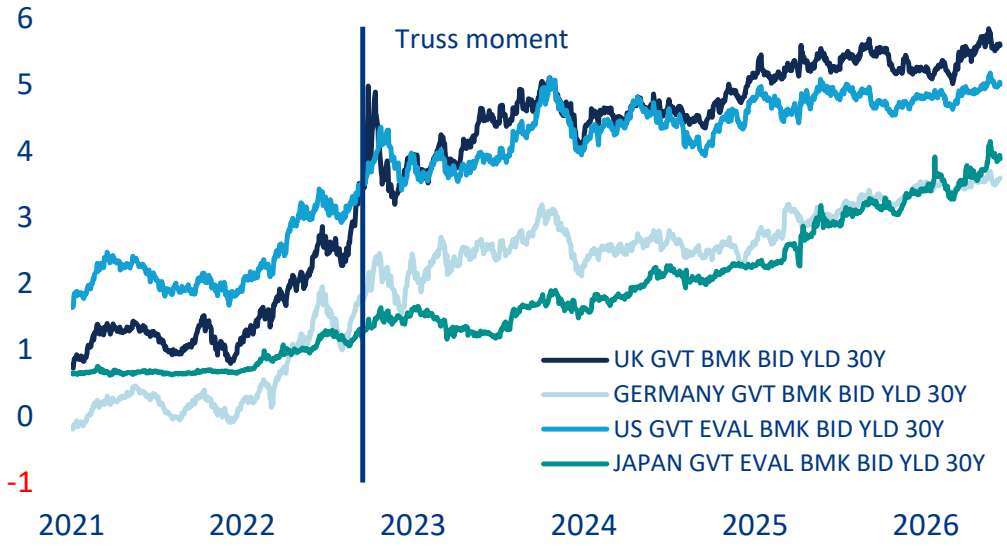
Sources: ILSEG Datastream, Allianz Research

The honest assessment is that London's clearing and derivatives franchise stopped growing into its natural trajectory rather than declined outright. Euro-denominated IRD trading surpassed US dollar-denominated instruments to account for the largest share of global IRD turnover in 2025 — growth that, absent Brexit, would have accrued disproportionately to London. The counterfactual loss is real even if absolute volumes remain strong. For the Gilt market, this matters through a second-order channel: a City that is less central to euro financial intermediation generates less natural structural demand for UK sovereign paper as collateral, reinforcing the shift toward a thinner, more price-sensitive foreign investor base.

The September 2022 fiscal episode is, in retrospect, the most consequential single event for the structural repricing of UK sovereign risk, more so than the referendum itself. It exposed the inherent fragility of a market dominated by concentrated, leveraged duration holders. The high-weighted average maturity of the Gilt stock (UK WAM is touching 13.5 year, against 7 year for Germany, or 6 year for US, at the end of 2025 according to the OCDE)) combined with the structural role of liability-driven investors and pension funds as dominant holders of long-dated paper, created a high vulnerability to duration shock and a self-reinforcing feedback loop that the Bank of England had to interrupt with emergency purchases of GBP65bn over 13 trading days. The episode established one structural fact that had not previously been priced: the central bank backstop for Gilts is conditional on fiscal credibility. Swap spreads, which had traded near zero prior to September 2022, moved to persistently negative territory, reflecting a banking sector constrained in its capacity to absorb newly issued sovereign paper, and a durable liquidity premium now embedded in the yield curve.

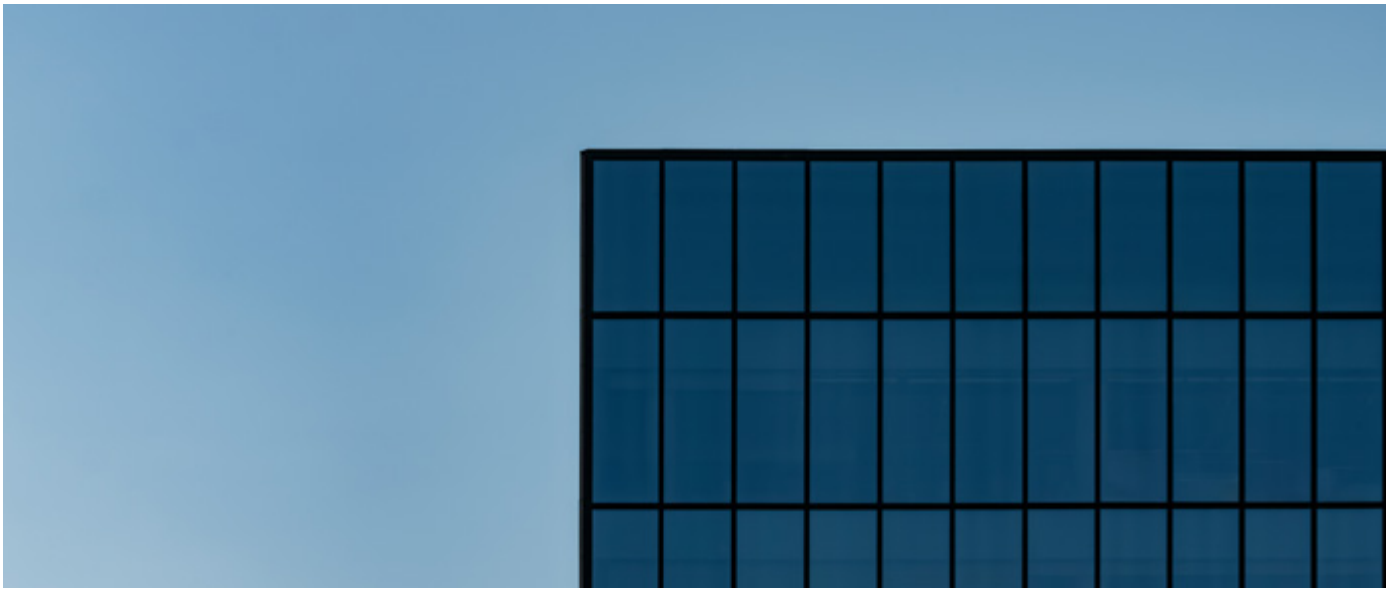
The transition from QE to quantitative tightening has compounded the vulnerabilities exposed in September 2022, but the causality is not purely mechanical. The Bank of England has pursued QT aggressively, in part as a deliberate signal to sovereign bond markets: a demonstration that institutional discipline had been restored after Truss. That signal has had a cost. The regime of scarce collateral and abundant reserves has given way to one of elevated Gilt supply and tighter bank funding conditions — GC rates now sit modestly above the BoE policy rate, consistent with a structural shift in money market. Banks depend more heavily on money market financing, reducing their capacity to absorb issuance and amplifying market sensitivity in stress episodes.

Figure 18: DM 30Y rates and GILT discount since the Truss moment



Sources: LSEG Datastream, Allianz Research

The BoE has credibly anchored the short end, what it has not recovered is control over the long end. Long-dated yields are increasingly set by supply dynamics, global uncertainty and term premia rather than by forward guidance or domestic macro anchors. US macro announcements — Fed decisions, Treasury supply, CPI prints — exert a more immediate and measurable effect on Gilt pricing than domestic budget decisions. This is the EMification dynamic in its precise formulation: not a loss of formal monetary sovereignty, but a structural compression of the market's capacity to price UK fundamentals independently of the global financial cycle. While this is a global phenomenon, the magnitude is strongly pronounced in the GILT market that exhibit a higher rate than the other DMs.



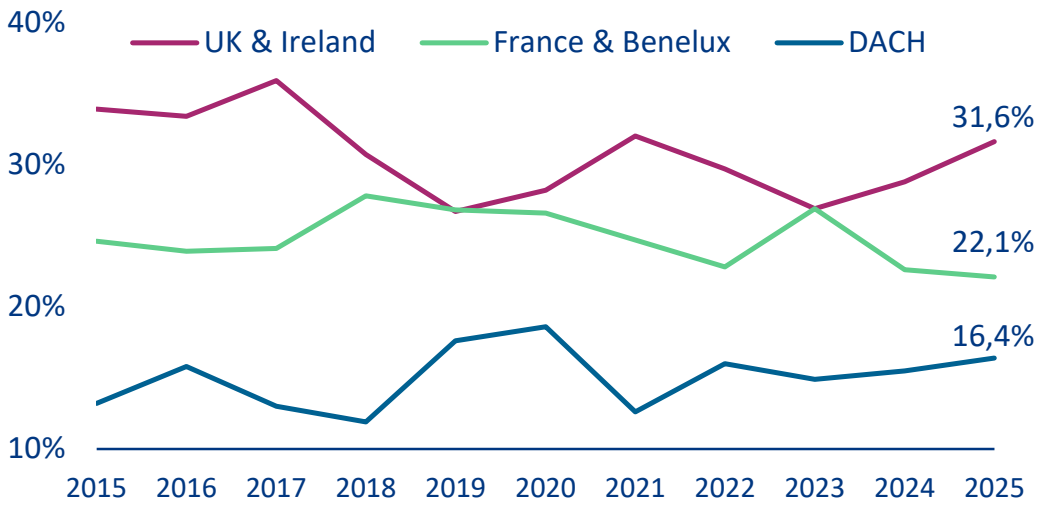
UK private equity market has lost its magic, low tech exposure prevails

A decade after the referendum, Brexit's imprint on UK private markets reads as a level shift that has now largely cleared the price. The UK is still Europe's dominant private capital hub, accounting for roughly one in five European deals and close to one in three fund closes, but it has stopped pulling away from the continent. The damage is real, concentrated and uneven: a one-off downshift in trend growth and relative attractiveness, since layered over by the pandemic, the energy shock and a higher-rate cycle that have blurred attribution. What remains is a market trading at a structural discount, increasingly financed from abroad, and now leaning on domestic policy to re-rate. Within that, the clearest bifurcation is in venture capital, the generalist fundraising base has hollowed out, yet the UK retains a relative structural edge in AI and deep-tech, where it continues to anchor the continent's largest rounds.

Brexit was a level shift, and it is now largely priced in. Estimates from Bloom et al. indicate that, by 2025, Brexit had reduced overall UK investment by around 12–18% relative to a no-Brexit counterfactual. Transmission ran through trade and labor frictions, the loss of passporting and equivalence, which pushed UK managers onto national private-placement regimes and EU-domiciled affiliates at higher operating cost, and through uncertainty itself, which depressed UK private equity volumes via a real-options "value of waiting" channel. Hundreds of financial firms have shifted staff, balance sheets and legal entities into the EU, re-anchoring fund servicing across Dublin, Luxembourg, Paris and Frankfurt and embedding a more multipolar European capital map. The discrete adjustment is behind us; what persists is a structurally higher cost of capital for UK risk assets.

Private equity proved resilient, increasingly as a US-funded value trade. The UK retains roughly a third of European private equity deal value, a position held through the post-referendum period, yet its deal value growth over the decade since the vote has materially lagged Germany and France, and Germany has displaced France as the continent's second market. The structural mechanism behind the UK's resilience is partly a discount story: compressed equity valuations relative to US peers have turned listed UK companies into prime take-private targets, drawing a sustained and disproportionately large share of US capital into the market, a pattern consistent across the post-Brexit cycle and the highest rate of US participation of any major European PE market. Buyout activity has increasingly defined the deal mix, reflecting both the take-private dynamic and the relative underrepresentation of growth equity in the UK versus continental peers.

Figure 19: The UK retains roughly a third of European private equity deal value.



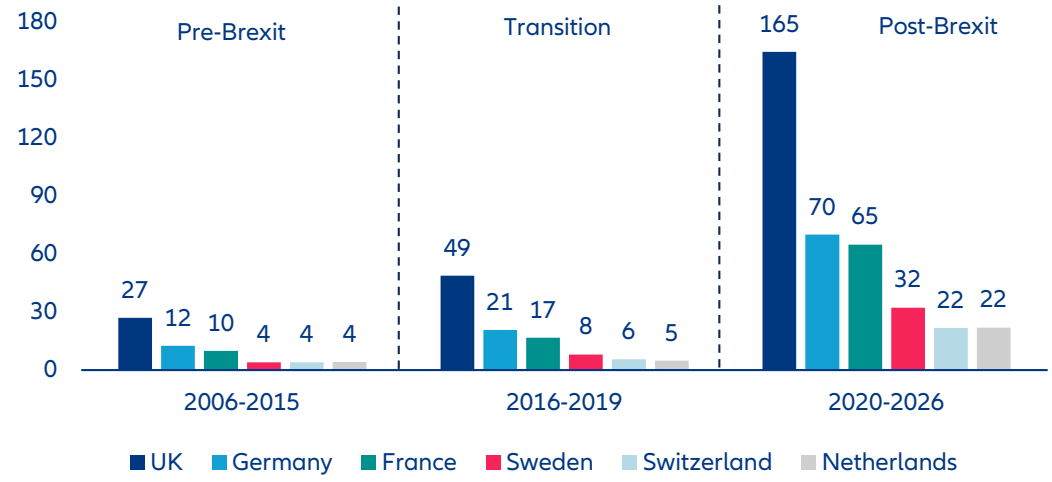
Sources : Pitchbook, Allianz Research

Notes: European PE deal value as a share of annual total by region.

The exit channel is the binding constraint, and policy has to be what clears it. Exit values have contracted sharply from the 2021-2022 peak and have been slow to recover, with disposals lagging deal formation and the ratio of PE-backed companies to exits widening to historically elevated levels , a backlog that accumulated across the rate-shock years and has yet to clear. The public listings market has been a structural drag, LSE has shed net listings across the post-Brexit decade, PE-backed IPO activity has been episodic rather than sustained and the equity re-rating visible in the FTSE 100 has yet to translate into a reliable exit route for private sponsors. Tax and domicile changes have added a directional headwind to manager incentives, reinforcing the pull of competing jurisdictions. Against that, the policy response is the most substantive in a decade, the Mansion House Accord targets GBP50bn of pension capital into private markets by 2030, PISCES provides an intermittent secondary venue short of a full listing and FCA deregulation is progressively lowering the post-Brexit compliance burden. Tentative green shoots are already visible in the exit data, PE exit value reached GBP20.9bn across 131 transactions in the first four months of 2026, pacing toward a record year by count, but the recovery is being led by buyouts rather than public listings, so the IPO channel most central to London's re-rating has yet to reassert itself.

The UK remains the most dynamic start-up ecosystem in Europe but the gap has narrowed since 2020. As Figure 21 shows, it still towers over Europe, drawing some USD 164bn of venture capital over 2020–2026, about two-and-a-half times Germany (68) or France (65) and roughly 44% of the six-country pool. Yet the UK's relative margin has quietly thinned since the referendum: its share of that pool eased from a 2016–2019 peak near 46% back to about 44%, and its lead over France narrowed from roughly 2.7x to 2.5x, as faster-growing rivals erupted around it. France and Germany remain the two heavyweight challengers, but the more telling shift is the rise of a second tier: Sweden, Switzerland and the Netherlands each pulled in between five and eight times more capital after 2020 than across the entire pre-Brexit decade (2006–2015) — Sweden, up eightfold to EUR32bn, has now overtaken both Switzerland and the Netherlands (22 each) to become Europe's third-largest hub. In short, Brexit left British innovation magnetic but no longer singular: the Continent is building its own pools of attraction, and the UK's edge, while still commanding, is slowly compressing.

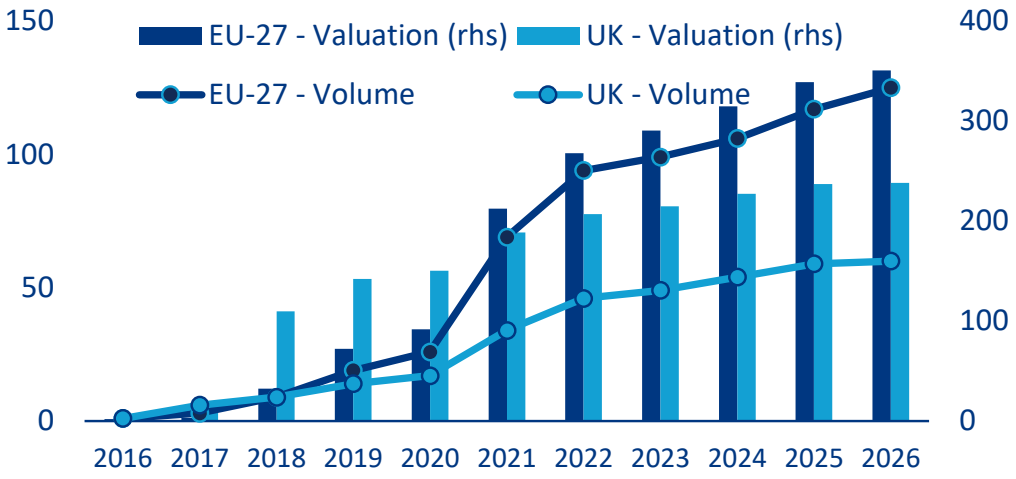
Figure 20: Venture capital investment in UK and top European peers between 2006 and 2026



Sources : Dealrooms, Allianz Research

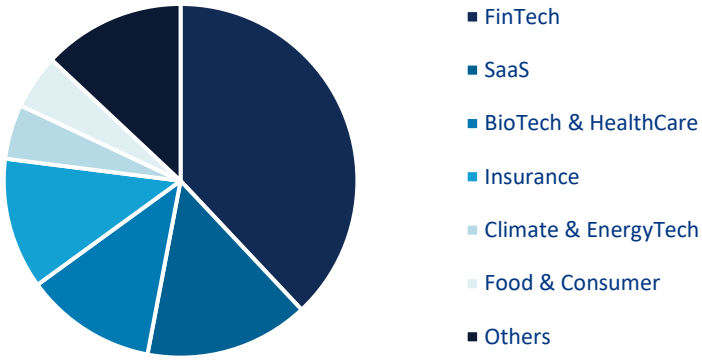
UK market dynamism hides a double concentration bias. With 60 active unicorns, the UK is the fourth largest market worldwide behind the US, China and India. However that fleet leans on a handful of sectors. Fintech alone makes up roughly 40% of the pack, with software, health and insurtech filling most of the rest; the deep-tech and frontier layers that build lasting advantage barely register. And value clusters even tighter than companies do – three names carry around 25% of capital raised over the past decade and initially 40% of the entire pool valuation. That fragility showed when the post-2021 sell-off hit. Having bet so hard on fintech and software, the very sectors that re-rated most brutally, the UK took the heaviest blow in Europe, unicorn fleet valuation being estimated in Q1 2026 at just 0.77x its last-round value, the most stressed major market, against a sturdy 0.97x in Sweden and 0.87x in Germany.

Figure 21: Venture capital investment in UK and top European peers between 2006 and 2026



Sources : CBInsights Allianz Research

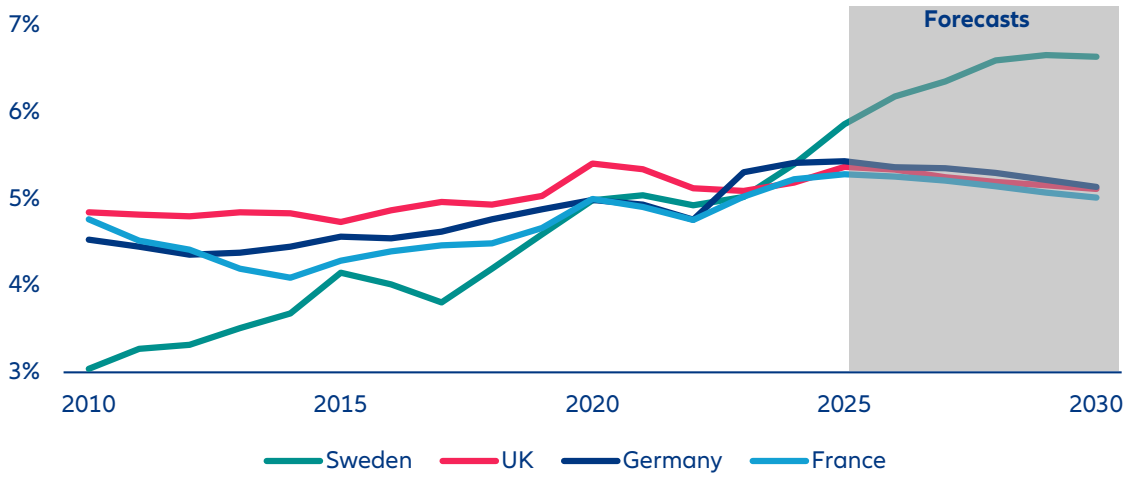
Figure 22: Sector breakdown of current unicorn ecosystem in UK (per volume)



Sources : CBInsights Allianz Research

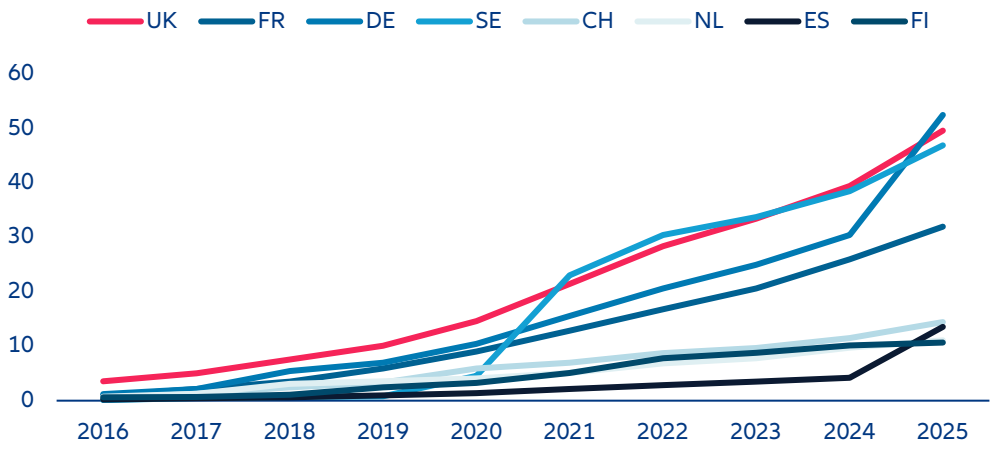
Diverging pattern: technology footprint is edging down in UK. ICT has grown into the UK's output more slowly than across the Channel — roughly 5.6% a year against 6% in France and 7% in Germany and Sweden — and the gap is widening, with Sweden breaking clear toward 6.5% of output by 2030 as Britain flattens near 5%. The causes compound. At home, finance, insurance and healthcare soak up the capital, starving the hardware and deep-tech that actually lift ICT's weight; the 2022 energy-and-inflation shock bit harder than on the Continent; and, cut off from EU structural funds, the UK now leans almost entirely on a private VC market that bankrolls software, not silicon. The deeper drag is structural: Europe's engineering schools feed a denser pipeline into mechanical and frontier-AI work, while the UK's own innovation watchdog warns its science-and-engineering skills shortage is now structural rather than That is the crux, as the Cambridge Industrial Innovation Policy's UK Innovation Report concludes, closing the country's scale gap demands complementary capabilities like skills, supply-chain depth and manufacturing capacity, not simply more capital. And with no homegrown ICT champion — its highest-ranked tech firm sits just 389th in global R&D spending — there is no locomotive to pull a cluster along behind it.

Figure 23: Evolution of the weight of ICT sector into some European economies (based on gross output)



Sources : Oxford economics, Allianz Research

Figure 24: Cumulative private investment into AI firms in European countries since 2016

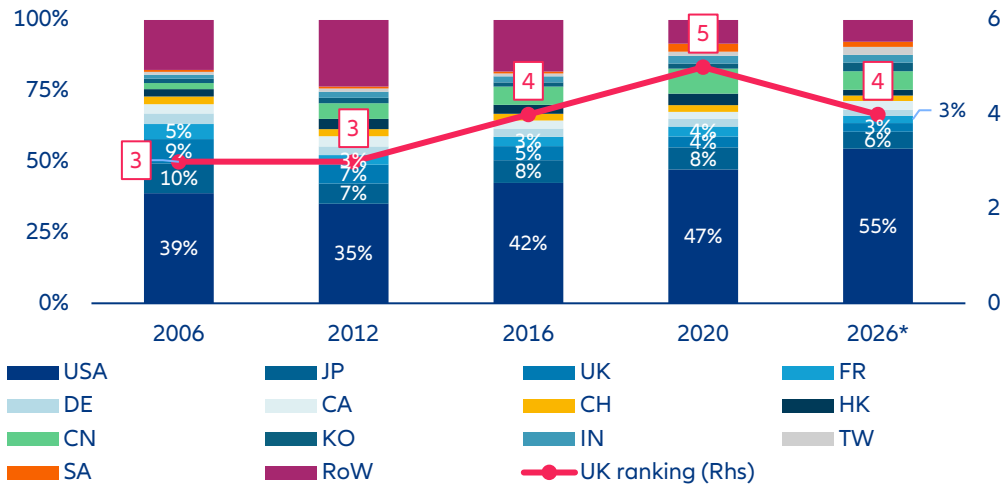


Sources :Center for Security and Emerging Technology (2026), Allianz Research

And the proof lands in AI itself. Narrow the lens to AI-specific capital and Britain's lead evaporates: Across 2020–2025 it drew around USD39bn, behind both Germany (USD45bn) and Sweden (USD46bn), with inflows growing just +21% a year lately against +24% in France and +37% in Germany – and a fast-rising Spain at +70%. The gap exposes where the UK sits in the value chain: strong in the materials layer – compound-semiconductor substrates, specialty chemicals – but absent from the parts that compound as comparatively to its European peers, the UK does not produce lithography machines or provide sovereign frontier-model and cloud services. London hosts among Europe's largest data-center fleets, but renting out the racks is not the same as owning the chips, models and clouds that fill them. That is the real verdict on Brexit-as-liberation: Far from a break-free moment to slip Europe's regulatory harness and chase the frontier, leaving the EU turned the UK inward — doubling down on the finance, insurance and software it already knew rather than the new domains where France, the Netherlands and Sweden are planting flags. The pandemic and the energy crisis weighed on the effort, but they cannot be the whole story, because the same storms crossed the Continent and its rivals emerged building, not retreating. The magnet still works – it is simply drawing capital into a narrower, more familiar field, while the frontier is mapped elsewhere.

The UK stock market has also lost its shine. The same loss of altitude shows up in public markets. London remains the world's fourth-largest equity venue by market capitalization — behind the US, China and Japan — but that perch is now crowded, with South Korea, Canada and Taiwan each circling at roughly 3% share. Trading itself hasn't dried up: daily turnover has actually risen since the 2016 vote, to about GBP4.8bn from GBP3.8bn, though that merely tracks a global pick-up in equity activity that ran hotter still in the US and parts of Europe. What has unmistakably shrunk is relative weight. The UK's share of global market cap nearly halved from around 8.5% in 2006 to 5% by 2016, then slid again to roughly 3% by 2026 — even as the US vaulted from 42.5% to 54.5% in the past decade alone. And British equities now trade at a 15–20% discount to their Eurozone peers, a gap that has barely budged in years.

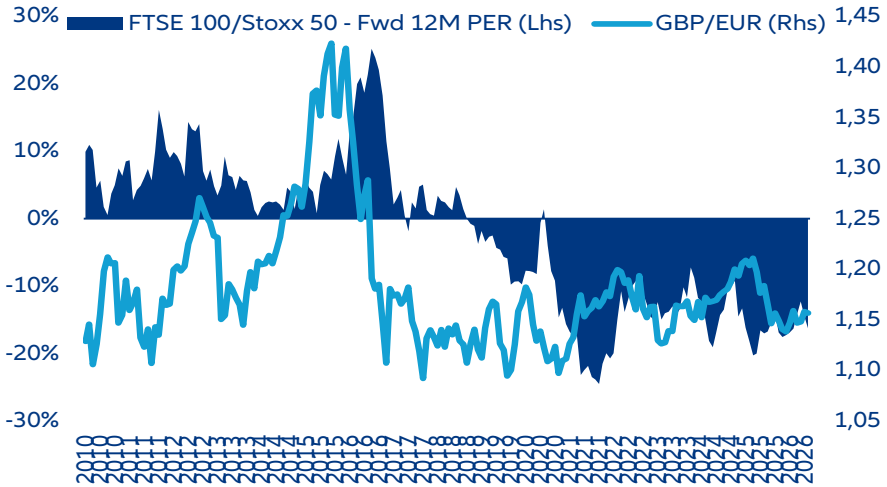
Figure 25: Market share of largest stock exchange place per market capitalization



Sources : LSEG Datastream, Allianz Research

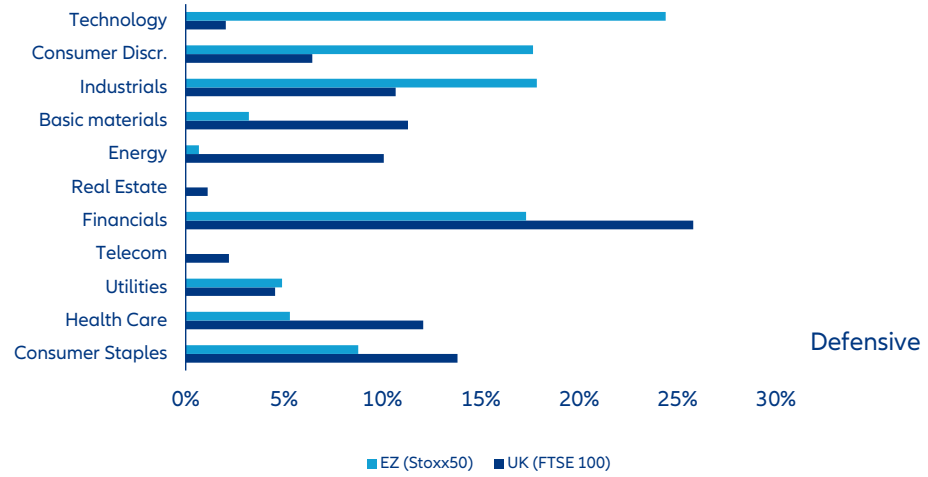
Persisting post-Brexit risk premia and low-technology profile burden stock attractiveness. The roots run deeper than Brexit — the slide was underway well before 2016 — but the divorce plainly didn't help. That lingering discount sits alongside a pound that never fully recovered against the euro or dollar, and a standing political-risk premium: global investors repriced UK assets downward after the referendum and never repriced them back. The bigger drag, though, is composition. The London index is structurally defensive — heavy in financials, energy, healthcare and staples, light on cyclicals — at the very moment markets have been relentlessly risk-on, powered by the AI trade. With technology barely 2% of the index, the UK simply lacks the exposure to ride that rally: its make-up cushions the blows in volatile, risk-off spells but caps the upside precisely when, as now, the world is reaching for growth. The equity market, in short, mirrors the innovation economy above it – safe, familiar and increasingly on the wrong side of where the frontier is moving.

Figure 26: Relative valuation of UK equity toward Eurozone peers



Sources : Dealrooms, Allianz Research

Figure 27: Sector classification differences

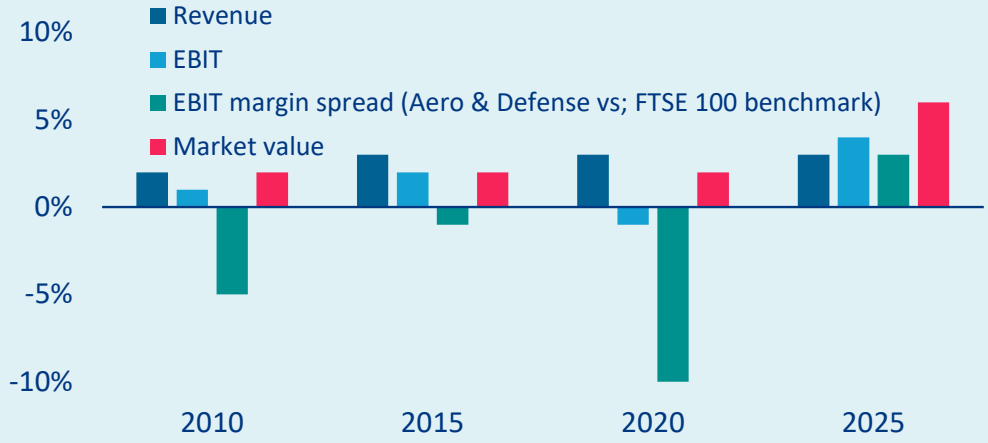


Sources :Center for Security and Emerging Technology (2026), Allianz Research

Box: Defense – Act or Lag

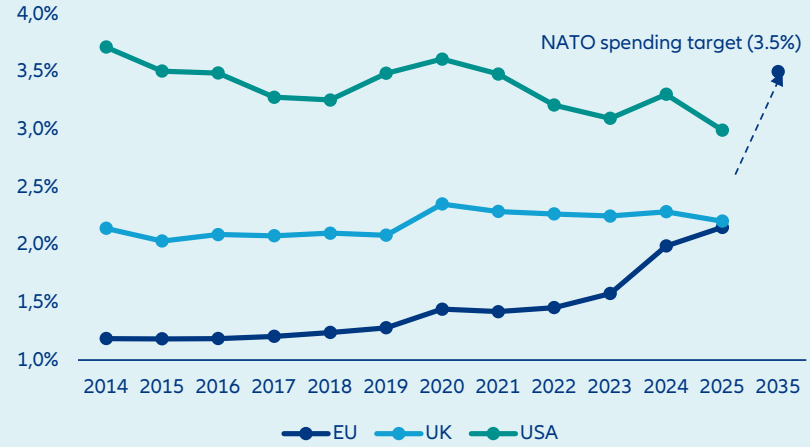
The Russia–Ukraine war handed European equity one of its scarcer assets — a genuine European growth story in which UK looks a lackluster against its peers. Continental names had a blockbuster 2025: the STOXX Europe Total Market Aerospace & Defence index returned roughly 68% over the twelve months into early 2026, taking the cumulative rally since Russia's February 2022 invasion to about 260%, with Rheinmetall — the rearmament proxy — up roughly 150% in 2025 alone and more than 1,000% above pre-war levels. Momentum has since cooled: the STOXX Europe Aerospace & Defence index is down ~1% year-to-date against ~5% for the STOXX 600 (late May 2026), and Rheinmetall sits about 38% below its January peak – a consolidation, not a reversal. The UK captures only a thin slice of that externality: core defense names in UK have roughly tripled their FTSE 100 market-cap weight since 2020, well ahead of the benchmark, but from such a low base that A&D stays a near-negligible index line. The US case is different again, and easily overstated as a Ukraine dividend: The S&P Aerospace & Defense Select index returned ~54% over the trailing year, comfortably ahead of the S&P 500 – but on an equal-weight basis that flattered smaller space and drone names) as much as giant domestic aerospace & aircraft. The marquee primes lagged: Lockheed fell ~13% over the trailing year and underperformed the S&P 500, leaving US primes at a discount to richly-rated European peers – a domestic budget-cycle trade (a ~USD1trn FY26 outlay) more than a war premium.

Figure 28: Weight of aerospace & defense core companies into FTSE 100 index benchmark (labeled in term of end fiscal 12-month trailing revenue, EBIT and market value)



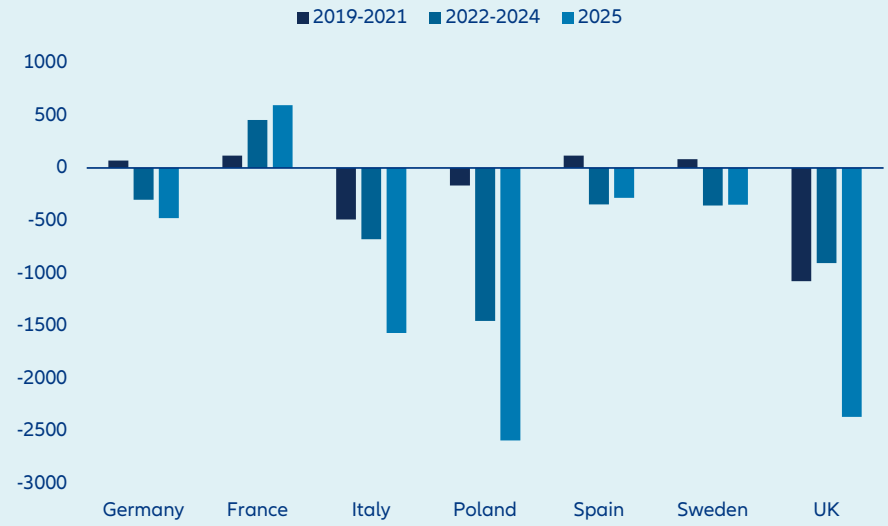
Source: LSEG Datatsream, Allianz Research

Figure 29: Evolution of military spending as % of GDP in EU, UK &



Source: NATO, Allianz Research

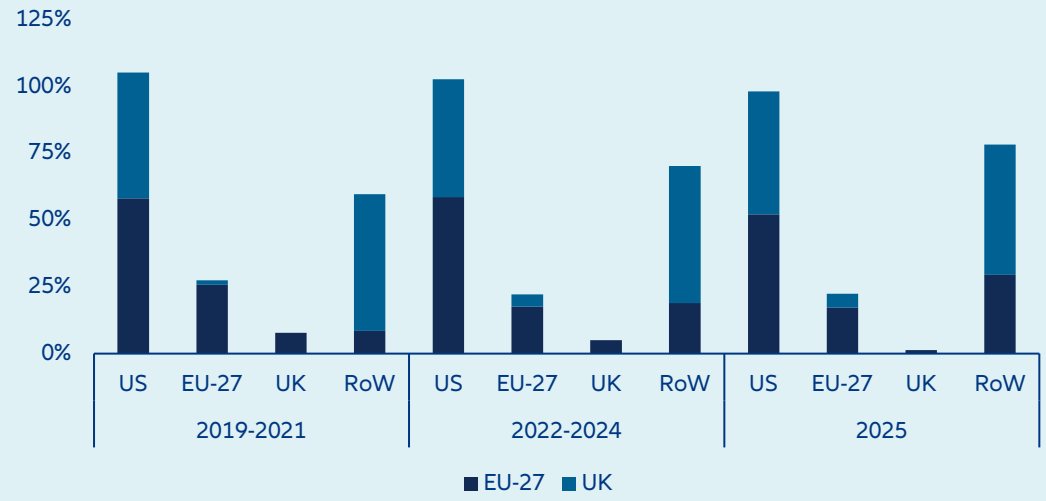
Figure 30: European countries trade balance with US in term of weapons and military equipment transfer (in mn of



Source: Sipri, Allianz Research

Neither war nor an American retreat drew Britain into Europe's defense fold. The chart tells it plainly: Across every window, including the 2022–24 war years, the UK's sourcing from EU-27 suppliers stays thin and by 2025 thins further toward the floor, while Britain remains a captive customer of US equipment, combat aircraft and munitions above all, for which it is Washington's only national "Level 1" industrial partner on the F-35, with roughly 15% of each airframe built in the UK. The corollary is a squandered windfall. Having opened negotiations to access the EU's EUR150bn SAFE rearmament facility after the May 2025 security pact, London walked away in late November over the entry fee and procurement terms — Brussels' demand reportedly ran to ~EUR6.75bn, even as Canada joined for around EUR10m — relegating UK firms to "third-country" status capped at 35% of any funded contract's value. And with the EUR150bn already parceled out to member states (Poland alone ~EUR44bn), that first-round ship has sailed. Global conflict handed Britain an open door to European defense-industrial integration and a multi-year demand pipeline to underpin its primes' earnings; it stayed welded to the dollar instead.

Figure 31: Regional distribution of arms & weapons imports by supplier breakdown (data labeled into millions of SIPRI trend-indicator values (TIVs))



Source: Sipri, Allianz Research

Stalling risks: funding constraints to hurt ambitious roadmap. On paper the trajectory is bold – 2.6% of GDP by 2027 en route to NATO's new 3.5% core target by 2035, 5% all-in — and the UK is embedded in a thick layer of partnership commitments, from AUKUS to the SAFE instrument and the trilateral GCAP fighter with Japan and Italy. In practice, a roughly GBP28bn funding gap and a Defence Investment Plan delayed several times have left those ambitions hostage to a Treasury unwilling to absorb more borrowing and a government wary that the tax rises needed to close the gap would render the agenda politically toxic. GCAP is the live illustration: lacking a long-term contract, the program has been running on a ~GBP686m bridge deal funding work only through end-June 2026, and frustration is rising in Italy and Japan that press UK government to offer funding guarantee. For the domestic base the signal is corrosive: immobilism today undercuts the case for capacity investment tomorrow and erodes the very argument primes need to attract capital – just as peers accelerate. The risk is not a reversal of intent but a creeping credibility gap between what Britain pledges and what it actually funds.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