Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Brexit Task Force:
October 2019 Update

Circulated to Commission Members on 15 October 2019

Contents

Executive Summary

- In the Q4 Quarterly Bulletin, the Central Bank published new forecasts for the main macroeconomic aggregates, prices and labour market variables under both a Brexit deal and no deal scenario.
- In the case that a deal can be agreed, the main impetus to growth over 2019 to 2021 is expected to continue to come from domestic demand driven by further growth in employment and incomes, though some moderation in employment growth is projected. GDP growth is projected to ease to 4.3 per cent next year and 3.9 per cent in 2021.
- In the no deal scenario most of the impact would be expected to occur in 2020, with the impact on employment lagging slightly in terms of timing. In this case, GDP growth is projected to slow to 0.8 per cent in 2020, before picking up to 1.9 per cent in 2021. Employment is projected to be 73,000 lower in 2021 and unemployment is forecast to rise to 5.8 per cent in 2020 and 6.9 per cent in 2021, over 2 percentage points higher in 2021 than in the deal scenario.
- UK real GDP contracted by 0.2 per cent quarter on quarter in Q2 2019, after having grown by 0.5 per cent in Q1. This was weaker than expected by market participants and represented the first contraction since 2012. Manufacturing output fell sharply in Q2, while growth in the services sector slowed down markedly to its lowest rate in three years.
- Throughout Q3, the Central Bank's Brexit Steering Committee has continued to focus on the mitigation (insofar as possible) of the near-term financial stability and consumer protection related risks of a no deal Brexit.
- In light of the actions taken prior to 29 March, there was little change in the status of the so called 'cliff edge' risks identified in previous reports. While continuing to monitor these risks closely, the Brexit Steering Committee also continued to focus on a number of other potential risks in Q3 […].
- [Omitted due to confidentiality].
- Banking supervisors have increased their engagement with banks (retail and investment) to re-assess their readiness for a no deal Brexit. On-going monitoring of credit, liquidity and market risks has intensified to enable timely identification of any emergence of risk.
- As Brexit date approaches, the Insurance Directorate has continued to ensure internal preparedness while also looking to the resilience of the financial system and of individual firms.
- The Securities Markets Supervision Division (SMSD) has continued to monitor fund activity since the extension of the Brexit deadline and has now stepped up its Brexit engagement with external

stakeholders with regard to new deadlines for submissions of fund documentation and increased the level of fund liquidity and market monitoring ahead of the new UK departure date.

- The continuation of the settlement of Irish corporate securities in the UK Central Securities Depository (Euroclear UK & Ireland) in a no deal Brexit outcome is effectively confirmed for a limited period i.e. until March 2021.
- The Minister for Finance and Public Expenditure and Reform and the Minister for Business Enterprise & Innovation (BEI) have obtained Government agreement to draft legislation that could facilitate the longer term transition of the Irish securities market to Euroclear Bank, Belgium.
- The impact of a no deal Brexit on the medium-term viability of credit unions remains unclear. Risks and commercial challenges in individual credit unions as a result of Brexit are likely to be particular to each credit union with some credit unions impacted more than others. RCU will continue to monitor the financial position of credit unions in assessing the impact a no deal Brexit may have on their medium-term viability.
- Since the last update was provided the operational risk environment resulting from Brexit has not changed significantly within the Central Bank. [Omitted due to confidentiality].
- [Omitted due to confidentiality].
- Special Topic 1 considers the impact of a hard Brexit on grocery prices in Ireland. In addition to short-term inflationary effects, a hard Brexit could exacerbate a number of structural features of Ireland and its groceries market that have caused Irish consumers to experience relatively high grocery prices over time.
- Special Topic 2 considers the short-term disruption to trade infrastructure in a no deal Brexit, where a transition period would not apply. This means there is not only the substantial impact of tariffs and non-tariff barriers, but substantial adjustment costs incurred as firms and administrative bodies in Ireland, the UK and other European countries would be required to implement all of the infrastructure, both administrative and physical, for trading with a third country in a very short period of time. The need to rapidly adjust to this new regime would impose significant costs on agents in the economy. The primary channels would be through logistics costs and the imposition of a new regime for sanitary and phyto-sanitary checks.

Overview

Following the Brexit referendum, the Central Bank's Financial Stability Committee (FSC) requested that a Task Force on Brexit implications be established on a permanent basis to monitor and assess developments in this area.[1] The Brexit Task Force (BTF) provides updated information regarding political, economic and financial market developments, risks arising for firms supervised by the Central Bank and issues arising for the Central Bank itself, in particular with respect to authorisations. Furthermore, each report selects a number of issues or policy questions related to Brexit and provides an in-depth examination of these areas.

The Report is structured as follows:
Section 1 provides a brief update of political developments; Section 2 provides an update in relation to the economic impact in Ireland arising from Brexit and an update on the UK economic environment and monetary policy; Section 3 provides an overview of contingency planning and cliff edge risks; Section 4 provides an update in relation to contingency planning across sectors; Section 5 considers organisational risks for the Central Bank; Section 6 provides an overview of authorisations activity; Section 7 contains a Special Topic on grocery prices in Ireland after Brexit, and Section 8 contains a Special Topic on the short-term disruption to trade infrastructure in a no deal Brexit.

[1] The following Divisions and Directorates are represented on the Brexit Task Force: AMSD, AMAI, BSAD, BSSD, CPD, FMD, FRG, FSD, GSD, IEA, IR, SMSD, INSA, MPD, ORD, Risk, SRD, PSSD, RES, and RCU. The report has also benefited from discussions with the Department of Finance (DoF). The Chair is the Director of Economics and Statistics, and the Secretariat is provided by MFD (Shane Byrne) and STSD (Andrew Hopkins).

1. Political Developments[2]

Article 50 Process State of Play

On 10 October, the Taoiseach met with PM Johnson. Both parties agreed they could see a pathway to a possible deal. Their discussions focused on the challenges of customs and 'consent'. They also discussed the potential to strengthen bilateral relations, including on Northern Ireland. They agreed to reflect further on their discussions and that officials would continue to engage intensively on them.

On 11 October, Michel Barnier met with Brexit Secretary Stephen Barclay and also briefed the EU 27 Ambassadors. Following these discussions, the EU Taskforce has concluded that there is now a basis for intensified discussions.

Ireland and the EU's position remains the same: there must be a legally operative solution in the Withdrawal Agreement that avoids a hard border on the island of Ireland, protects North-South cooperation, the all-island economy and the Good Friday Agreement in all its dimensions, and safeguards the integrity of the Single Market and Ireland's place in it.

The next European Council will be held on 17/18 October.

UK Developments

Since the election of Boris Johnson as Prime Minister on 24 July the political situation in the UK has continued to evolve. There have been a number of significant events of note including the 4 September defeat of the Government on a motion to avoid a no deal Brexit on 31 October, and the 24 September Supreme Court ruling that the proroguing of Parliament until 14 October was unlawful and therefore void.

The 4 September motion on which the Government was defeated requires the Government to seek an extension to Article 50 until 31 January 2020, if the House of Commons has not approved a deal, or has not approved leaving the EU without a deal, by 19 October. The motion was supported by 21 Tory MPs, who have since lost the part whip, which means that PM Johnson now leads a minority Government.

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[2] Our thanks to the Department of Finance for providing the background information on the latest political developments.

Following the 24 September UK Supreme Court ruling, Parliament reconvened on 25 September. On 8 October a short prorogation was called. The new parliamentary session began on 14 October, with a Queen's speech that set out the Government's legislative agenda.

Domestic Developments

The Irish Government assessment continues to be that the risk of no deal Brexit remains high and planning for a no deal Brexit has the highest priority across Government.

The Government's Contingency Action Plan Update, published on 9 July, reflects the extensive work which had taken place on a whole-of-Government basis and at EU level to prepare for a no deal Brexit. It also set out the next steps to be taken up to 31 October.

Key areas for work identified in the Action Plan update include preparing for Budget 2020, additional infrastructure for ports and airports, and a new phase of the Government's Brexit communications. This work is being progressed with the highest priority across Government.

Budget 2020 was published on 8 October and is based on a No Deal as the central assumption. It sets out a package of over €1.2 billion (excluding EU funding) to respond to Brexit, including contingency Brexit funding which will be activated only in the event of a No Deal.

EU Developments

The European Commission launched its sixth Brexit Contingency Communication on 4 September. It proposes the extension of key unilateral EU no deal measures into 2020 in the areas of road haulage (to 21 July 2020) and aviation (to 24 October 2020), on the basis of reciprocation by the UK. The Communication also proposed the extension of contingency measures in respect of Fisheries and the EU Budget to the end of 2020. Both are dependent on UK Government policy actions. There were two new measures proposed in the Communication to extend the scope of two existing EU Funds, the EU Solidarity Fund and the European Globalisation Adjustment Fund to provide support in the case of a no deal Brexit.

2. Economic Background

2.1. Summary of Latest Irish Projections[3]

Since the last Brexit Task Force report, the Central Bank revised up its forecasts for economic growth due to continued employment growth and stronger consumer spending. The central projection still assumes that a hard Brexit does not occur on 31 October, and a deal that includes a transition period until the end of 2020 is agreed. However, given the increasing risk that the UK will leave the EU without a deal, there will be a negative effect on consumer sentiment and the investment decisions of firms throughout the second half of 2019.

Based on the agreement of a transition period to end-2020, the Central Bank's central forecast is that underlying economic activity will continue to grow at a solid pace over the coming years, although the rate of growth may moderate in 2019 and 2020. This moderation is based on the weakening global economic environment, as well as the limiting effect of supply constraints as the economy approaches its productive capacity. GDP is expected to grow by 5 per cent in 2019 and 4.3 per cent in 2020.

Impact of a Disorderly no deal Brexit on the short term forecast[4]

If a no deal Brexit were to occur on 31 October, it would represent a significant downward revision to growth expectations. Estimates of the impact of a no deal Brexit published in January 2019 suggested that output growth would be reduced by 4 percentage points in the first year. Given that the possible date of Brexit is 31 October of this year, most of the impact will occur in 2020. Applying this shock to the Central Bank's current forecasts results in the alternative forecast shown in Table 2.1.1, below.

Table 2.1.1: Impact of Disorderly Brexit on 2019 and 2020 Growth Rates

	Baseline		No deal	
	2019	2020	2019	2020
GDP (%)	5.0	4.3	4.7	0.8
Employment (%)	2.4	1.5	2.1	0.2

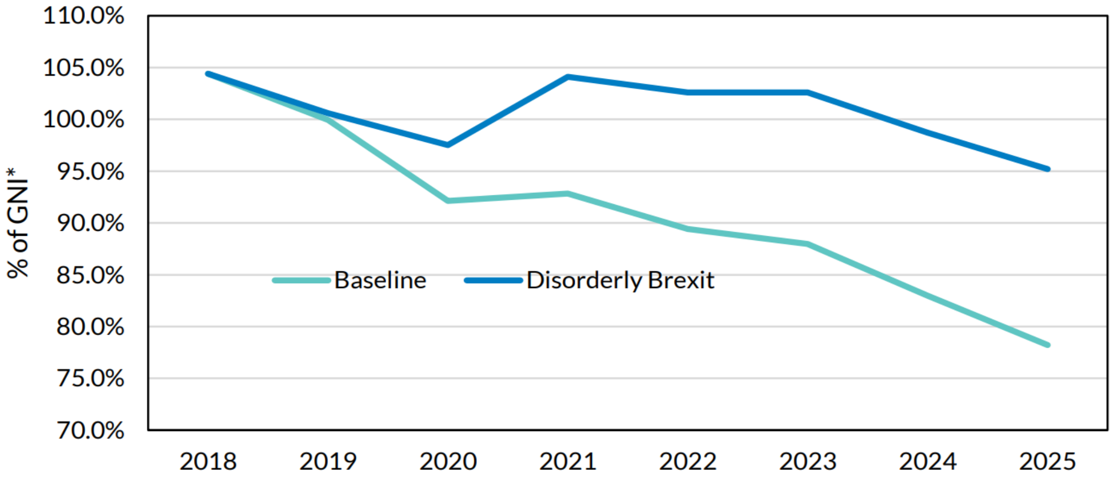
Source: Central Bank of Ireland Quarterly Bulletin 4, 2019.

[3] Prepared by Irish Economic Analysis Division (IEA).

[4] The estimates presented in this section are subject to a greater deal of uncertainty than is typically associated with economic forecasts, given the unprecedented nature of the shocks.

Our estimates suggest that by the end of 2021, there would be 73,000 fewer jobs in the economy compared to the baseline projection. In addition, the fall in output and employment would put pressure on the public finances. In a recent *Economic Letter,*[5] it is estimated that the reduction in revenue and increase in unemployment related expenditure would worsen the general government balance by about 2 percentage points in the long-run. The larger budget deficits would lead to higher Government debt levels, with the debt to income ratio projected to be 17 percentage points higher under a no deal scenario (Chart 2.1.1).

Chart 2.1.1: General Government Debt in a Disorderly Brexit, % of GNI*



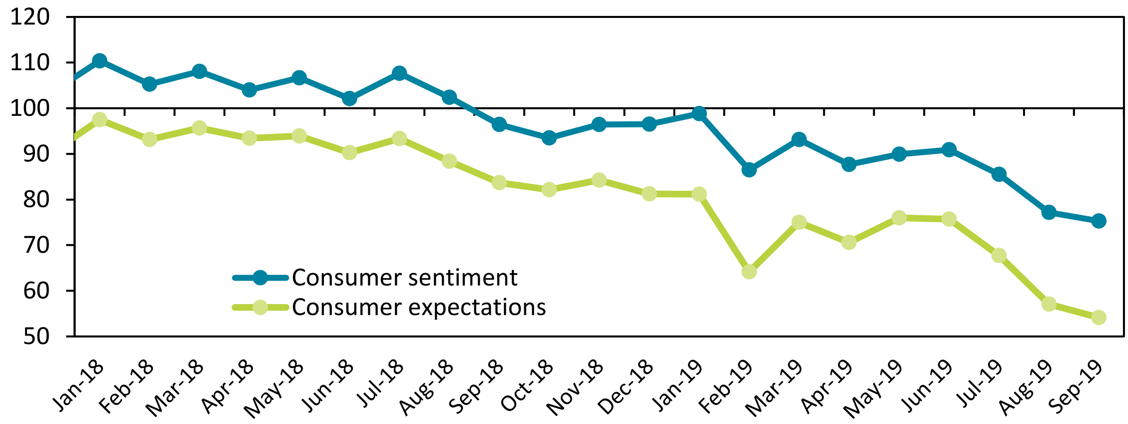
Source: Conefrey et al. (2019)

Sentiment

The effect of Brexit on consumer sentiment had been somewhat difficult to discern given the counterbalancing effects of low unemployment and rising incomes. The latest data, however, confirm a significant fall in Irish consumer sentiment as we approach 31 October (Chart 2.1.2).

[5] Thomas Conefrey, Rónán Hickey, and Graeme Walsh (2019) Debt and Uncertainty: Managing Risks to the Public Finances, *Economic Letter No. 11, 2019.*

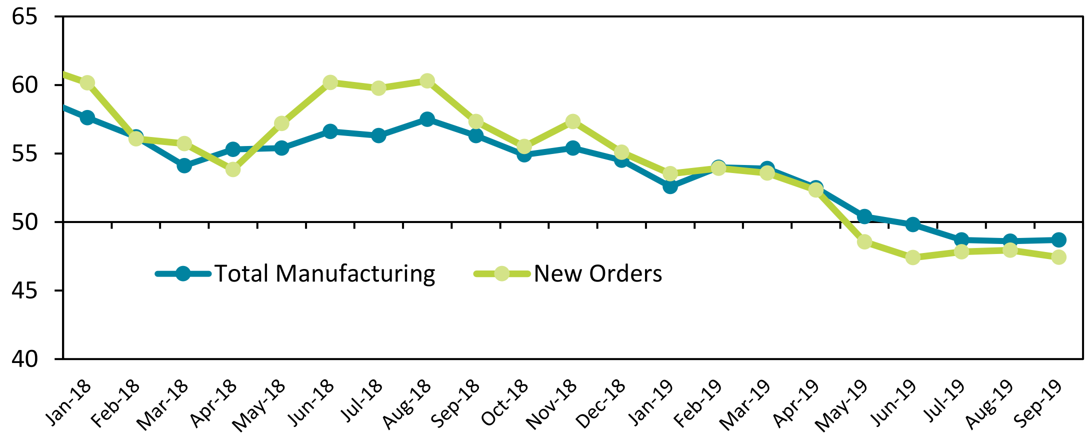
Chart 2.1.2: Irish Consumer Sentiment since 2018



Source: KBC Consumer Sentiment Indices

Consumer sentiment now stands at its lowest level since November 2013, with an increasing proportion of those surveyed worried about job losses and a future deterioration in their personal finances. The proportion of households reporting that they were willing to make major purchases also declined, suggesting that Brexit related uncertainty is affecting purchasing decisions. While there has been a continued downward trend in recent months, sentiment could greatly improve if a no deal Brexit is avoided.

Chart 2.1.3: Irish Business Sentiment since 2018



Source: AIB PMI, Seasonally adjusted

In terms of business sentiment, the AIB manufacturing PMI remains in contractionary territory, having risen by 0.1 points to 48.7. This represents the fourth consecutive month of worsening conditions. The New Export Orders series fell by almost two index points this month to stand at 46, its lowest level since 2009. The manufacturing sector continues to add to employment, but Brexit combined with the slowdown in global manufacturing is negatively affecting Irish firms.

2.2. UK Macroeconomic Update & Monetary Policy

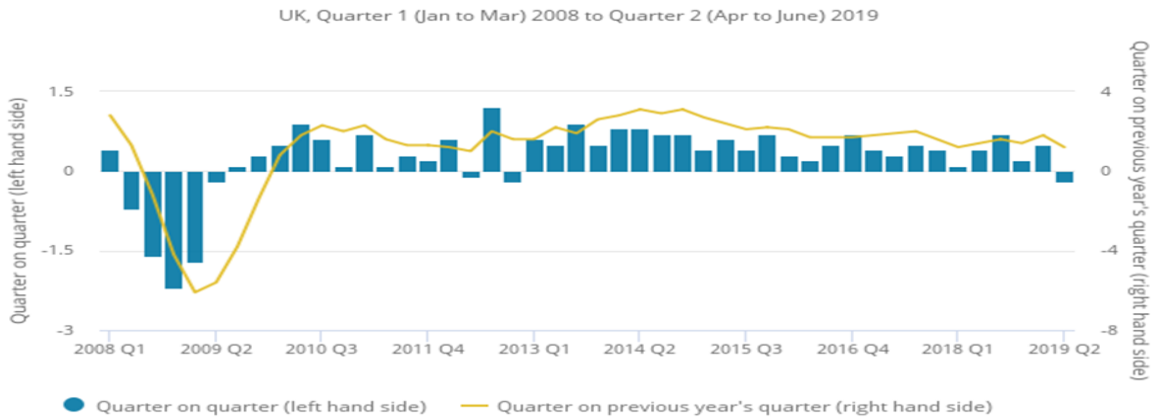
UK Macroeconomic Update

UK real GDP contracted by 0.2 per cent quarter on quarter in Q2 2019, after having grown by 0.5 per cent in Q1. This was weaker than expected by market participants and represented the first contraction since 2012 (Chart 2.2.1). Manufacturing output fell sharply in Q2, while growth in the services sector slowed down markedly to its lowest rate in three years.

Uncertainty and stockpiling related to the original Brexit date seem to have been the main drivers of the volatility experienced by the UK economy. Stockpiling contributed positively to growth in Q1 ahead of the April 29 Brexit deadline, and then the impact was negative in Q2.

The labour market remains tight with unemployment falling to 3.8 per cent in the three months to May, below the assessed equilibrium rate of 4.25 per cent.

Chart 2.2.1: UK Real GDP Growth



Source: Office of National Statistics (ONS)

Bank of England (BoE) Monetary Policy

The BoE's Monetary Policy Committee (MPC) voted unanimously to hold the Bank rate at 0.75 per cent at its September meeting and to maintain the current level of government bond purchases at £435bn and corporate bond purchases at £10bn. The BoE struck a generally dovish tone, warning that as long as the current political uncertainty persists, there is a bigger risk that it would hamper growth and dampen inflationary pressures. In addition, subsequent comments from the BoE's MPC member, Michael Saunders, noted that even if the UK avoids a no deal Brexit, rates may still need to be cut. The market pricing on the probability of a BoE rate cut by the end of the year has risen from 16 per cent to 30 per cent over the period.

2.3. Financial Market Developments

Financial markets started to price in a greater risk of a no deal Brexit with Boris Johnson's leadership victory in late July, as he stated unequivocally that he intended for the UK to leave the EU by the 31 October deadline. Table 2.3.1 below illustrates movements in sterling and selected equities over the period.

Table 2.3.1: Sterling and equity price movements (21 May – 11 October)

	21-May-19	11-Oct-19	Change
FX			
GBP/USD	1.27	1.25	-1.49%
EUR/GBP	0.88	0.88	0.19%
Equities			
FTSE100	7329	7190	-1.90%
Bank of Ireland	5.25	3.97	-24%
AIB	4.07	2.91	-29%

Source: Bloomberg

Sterling declined against the US dollar (USD) over the period by approx. 1.5 per cent, but made modest gains against the euro owing to the monetary policy easing by the ECB's Governing Council in September. Sterling had declined more steeply against both the euro and the USD in August arising from increased concerns of a disorderly Brexit. However, the passage of a bill by the House of Commons to prevent a Brexit no deal and the Supreme Court's overturning of the PM's suspension of Parliament have diminished market expectations of a disorderly Brexit, which in turn provided some renewed support to sterling. Sterling options are discounting less long-term volatility, although implied volatility on short dated options that span the October deadline are more elevated.

The FTSE 100 fell by just under 2 per cent over the period, having recovered since August when the index had declined by as much as 9 per cent from its peak in July. The more recent re-pricing of UK assets reflects a reduced level of Brexit uncertainty. However, AIB and Bank of Ireland (BoI) posted sharp declines in share prices of 29 and 24 per cent respectively against a weak earnings backdrop, with BoI noting that Brexit uncertainty amongst other bank specific factors (including cost base and IT infrastructure investment) is presenting the bank with challenges in generating income and loan growth.

UK Gilt yields fell on a flight to quality bid amid increased expectations of rate cuts from the BoE. Table 2.3.2 below illustrates movements in the 2 and 10-year Gilt yields over the period, which declined by 26 and 47 basis points respectively.

The Irish 10-year spread to Germany tightened over the period, by 7 basis points to 0.52 per cent. Irish bond spreads have in general been relatively stable; they have marginally underperformed their French and Belgian 10 year equivalents by 1 and 7bp respectively.

Chart 2.3.2: Sterling and equity price movements (21 May – 11 October)

Gilts	**21 May 2019 (%)**	**11 October 2019 (%)**	***Change (basis points)***
2-year Gilt yield	0.73	0.47	-26
10-year Gilt yield	1.08	0.61	-47
Irish 10 year spread over Germany	0.59	0.52	-7
Irish 10 year spread over France	0.20	0.21	1
Irish 10 year spread over Belgium	0.11	0.178	7

Source: Bloomberg

3. Contingency planning and cliff edge risks[6]

Throughout Q3, the Central Bank's Brexit Steering Committee continued to focus on the mitigation (insofar as possible) of the near-term financial stability and consumer protection related risks of a no deal Brexit. A key focus of the Committee is to ensure that a 'one Bank' view is being taken to identified risks, to ensure mitigating actions are being progressed in a timely manner and to address any roadblocks to completing these actions.

On the basis of the Brexit work that has been done domestically and at EU level from a policy and legislative perspective and, crucially, the work of the last decade to drive a significantly more resilient financial system, the immediate cliff-edge financial stability risks of a no deal Brexit are considered to be broadly manageable at this point. That said, it is recognised that this eventuality would be challenging for all firms operating in Ireland and that there will inevitably be some negative impact on consumers where firms have not put suitable plans in place, failed to secure the necessary authorisation to continue to conduct business in Ireland, or chosen no longer to provide financial services here.

In terms of the status of the cliff edge risks outlined in previous reports, there was very little change during Q3 as significant efforts had been made to ensure appropriate mitigations were in place for these risks by the initial Brexit deadline of 29 March. That said, and as outlined previously, the extension of the Brexit date to 31 October erodes the agreed transition period and temporary equivalence periods put in place at EU level to mitigate the cliff edge risk pertaining to UK Central Counterparties (CCP) and the Central Securities Depository (CSD). In the absence of any indication from the European Commission at this point that it will extend these temporary equivalence decisions, increased action is required by industry to ensure appropriate measures are taken to mitigate these risks over the more compressed time period available (i.e. before the expiration of the relevant transitional equivalence decisions). Another risk highlighted previously, relating to the further extension of the Brexit date, was the loss of impetus for firms to build out their operations in line with their conditions of authorisation. The Central Bank has continued to engage with firms to ensure that they are operating in line with its supervisory expectations in terms of asset transfer and client migration, and progress has been made on this front in recent weeks.

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[6] For a discussion of key cliff-edge risks identified as part of the Central Bank's Brexit preparations, please see the March 2019 Brexit Task Force Report.

In light of the mitigants now in place for the identified cliff edge risks[7] (and while the Central Bank continues to monitor these risks closely) […].

[Omitted due to confidentiality].

[Omitted due to confidentiality].

[7] Lack of access to UK CCPs (mitigated by a temporary equivalence decision until March 2020); settlement of IE securities on UK CSD (mitigated by temporary equivalence decision until March 2021); service continuity for insurance contracts (mitigated by domestic legislative temporary run off regime); and disruption to cross border fund management services (with the delegation of portfolio management aspect mitigated by ESMA MMoU).

4. Sectoral Update

4.1. Banking

In preparation for end October, banking supervisors have increased engagement and monitoring of key risk indicators to enable timely identification of any emergence of risk. This should allow for timely supervisory action, if needed in the event of a no deal Brexit.

This has focused on:

I. Operational readiness plans for the period surrounding a no deal Brexit;
II. Refreshing our assessment of the risks from cliff-edge effects arising from a no deal Brexit;
III. The Central Bank's actions and plans to manage credit, liquidity and market risks in the period leading up to and following a no deal Brexit;
IV. Requesting additional regular quantitative and qualitative data from retail banks and investment banks to allow for the timely assessment of risk development;

[Omitted due to confidentiality].

Finally, within Banking Supervision, internal operational readiness plans are being revisited.

4.2. Insurance

As the next Brexit date approaches, the Insurance Directorate has focused on internal preparedness as well as the resilience of the overall financial system and the resilience of individual firms. This has been done through continued engagement with firms, EIOPA and the UK and Gibraltar supervisors.

At a European level, the EIOPA Multilateral Memorandum of Association (MMoU), adopted in February, was signed at the end of March. [Omitted due to confidentiality]. The Central Bank intends to comply with the EIOPA Recommendations for the insurance sector should the UK withdraw from the EU in entirety.

Internally, the Insurance Directorate has continued to host Brexit Insurance Supervisory Co-ordination Group (BISC) meetings with Legal, Consumer Protection and Policy representatives. No new sectoral risks or issues have emerged since the delay to Brexit.

Authorisations

[Omitted due to confidentiality]

Contingency planning outwards: Ireland to UK

As discussed in previous reports, the Temporary Permissions Regime[8] (TPR) has addressed the issue of UK contract continuity. The Prudential Regulation Authority (PRA) visited the Central Bank in September to brief those firms intending to enter the TPR and submit a branch application. There are also alternative methods to the TPR, such as the Financial Services Contracts Regime, and these have been discussed in previous reports.

[Omitted due to confidentiality]

Contingency planning inwards: UK/Gibraltar to Ireland

In order to mitigate contract continuity risks the Domestic Temporary Run-Off Regime (TRR) was passed by the Oireachtas in March. All aspects of this regime have been finalised in terms of the application process, processing of the notifications and on-going supervision of same. The Insurance Directorate is currently ensuring that the regime is ready for implementation immediately after Brexit.

4.3. Asset Management

Supervisory engagement: Analysis of firms' preparation for Brexit (including a hard Brexit)

Supervisors in the Asset Management and Investment Banking Directorate (AMIB) continue to engage with firms to understand any potential business impact arising from the delayed Brexit timelines and the potential for a no deal Brexit. A Brexit preparedness questionnaire was issued to firms in August seeking an update on a number of Brexit risks, including: any emerging risks that have been identified and how they are being mitigated; the impact of Brexit Cliff Edge risks; potential impact on Clients and Technology resilience. The responses have been received and are being assessed by the supervisory teams. In addition, supervisors are engaging with the newly authorised firms to understand their plans for commencing activity and any alterations to business migration plans as a consequence of the delay to Brexit.

[8] EEA Passport Rights (Amendment, etc., and Transitional Provisions) (EU Exit) Regulations 2018 legislation.

Supervisory engagement in relation to Brexit will continue in the lead up to the 31 October deadline, with a particular focus on hard Brexit planning, the share trading obligation requirements, and any emerging risks.

ESMA Engagement

The ESMA Supervisory Co-ordination Network (the 'SCN') continues to meet regularly to discuss cases of authorisation requests and any supervision/enforcement issues arising from investment firms, asset managers and trading venues seeking to relocate from the UK. The Director of Asset Management and Investment Banking represents the Central Bank at the SCN. Key issues for ESMA include, inter alia, the risk of letter-box entities, substance in the EU, governance, significant outsourcing or delegation that lead to a substantial part of the activities being undertaken outside the EU and the risk of significantly different treatment between entities across the EU.

National Competent Authorities (NCAs) are invited to present live cases to the SCN on an anonymised basis for discussion. NCAs will then provide further updates to keep the SCN informed as applications develop. The Central Bank most recently presented at the September SCN meeting on two authorisation cases. AMIB has now presented on the majority of its applications and will continue to engage with EU NCAs on new authorisation cases.

Authorisations

[Omitted due to confidentiality].

4.4. Securities and Markets

The Securities Markets Supervision Division (SMSD) has continued to monitor fund activity since the extension of the Brexit deadline and has now stepped up its Brexit engagement with external stakeholders with regard to new deadlines for submissions of fund documentation and increased the level of fund liquidity and market monitoring ahead of the new UK departure date.

In August SMSD issued correspondence to Irish investment funds who are affected by the loss of the Fund Management Company (FMC) passport for both UK UCITS Management Companies and Alternative Investment Fund Managers (AIFMs), reminding them of their obligations in this regard and the new Central Bank deadlines which will apply to funds seeking to move their management away from UK entities in the event of a no deal Brexit. All funds who are currently managed by UK FMCs will be required to inform the Central Bank of their intentions by early September. [Omitted due to confidentiality].

Also in August, a number of communications were issued to remind stakeholders of the need to update relevant documentation ahead of the new Brexit deadline. In the context of investment funds, Irish Funds were contacted to remind funds that prospectus amendments reflecting the UK's change in status (to being a non-member of the EU) must be submitted to the Central Bank by the end of September. In the area of debt and equity prospectus applications, SMSD has advised stakeholders that Brexit applications must be submitted by 6 September in order to allow sufficient time for scrutiny.

As previously, SMSD continues to monitor the liquidity of Irish investment funds, monitoring for the emergence of systemic risks in the funds industry associated with the UK's departure. On 7 August a letter was sent to the funds outlining their responsibilities with respect to their liquidity, specifically noting that it is critical that the execution of the liquidity risk management framework for each fund is calibrated to take into account dealing frequency, investment strategy, portfolio composition and investor profile on an ongoing basis.

Similarly SMSD continues to monitor general market activity with analysis circulated to SMS management and relevant staff on a daily basis. Market developments are then discussed each week through a broad forum of management and staff across various teams.

4.5. Consumer Protection Supervision

Brexit - Freedom of Services (FoS)/ Freedom of Establishment (FoE) Inwards – General Update

In the course of the Central Bank's preparation for a no deal Brexit scenario, there has been significant engagement with UK and Gibraltar firms operating in Ireland on a FoS and FoE basis. Much of this engagement is focused on gauging the level of preparedness of these inward passporting firms and ensuring they have carefully assessed their obligations to existing and prospective customers, and taken any necessary actions to mitigate potential risks that may arise. Also reminding firms that they must continue to provide clear information to customers whose contracts or services may be affected, as soon as that information becomes available to them. To date, the response rate of firms has varied across sectors. Consequently, the extension of the Brexit withdrawal date to 31 October has provided an additional window of time to address this, and the Central Bank continues to employ a risk-based approach to assessing the Brexit preparedness of these firms across sectors, and is also working closely with the relevant ESAs in this regard.

Brexit - FoS Inward Banks – Specific Update

The Central Bank has had extensive engagement with UK and Gibraltar firms operating in Ireland on a FoS and FoE basis, including inward passporting credit institutions. This engagement has continued to focus on the level of preparedness of these firms for a hard Brexit, including their contingency plans to minimise Brexit-related risks to consumers and associated communications with consumers. The Central Bank has also continued to engage with UK regulatory authorities.

As at end August, the majority of credit institutions selling financial products and services from the UK to Ireland, are implementing plans to mitigate the risks to Irish customers. However, some risks remain, including potential for disruption to, or discontinuation of services, or where firms engage in unauthorised activity, loss of access by consumers to the Irish Consumer Protection Framework or the Financial Services and Pensions Ombudsman. The Central Bank will continue to press these credit institutions to minimize these risks […].

We are currently considering the use of our regulatory powers on a case-by-case basis if a firm continues to conduct business in Ireland without the required authorisation.

The Central Bank continues to iterate that it is the responsibility of each firm to satisfy itself, including through obtaining advice from its legal advisors, of its licencing and regulatory obligations under Irish financial services legislation, and (where relevant) seek alternative authorisations.

Authorisations Update - Payment & Electronic Money Institutions and Retail Intermediaries

Consumer Protection Directorate (CPD) is responsible for the authorisation and supervision of Payment Institutions (PI), Electronic Money Institutions (EMI) and Retail (insurance and mortgage credit) Intermediaries (RIs). Since the June 2016 UK referendum, CPD has seen a significant increase in applications for authorisation received as a result of Brexit.

[Omitted due to confidentiality].

Since August 2019, all applicants in the assessment phase of the authorisation process have been categorised as either ‘likely’, ‘possibly’ or ‘unlikely’ to be authorised by 31 October. Any applicant who is considered ‘unlikely’ to be authorised by this date has been so advised to enable them to consider whether they require any further Brexit contingency planning. The categorisation of all applicants will be assessed on an on-going basis with the ‘unlikely’ to be authorised firms being so advised as early as possible. All firms whose application remains in the assessment phase of the authorisation process will be reminded of outstanding issues in respect of their application and the importance of addressing any such issues as soon as possible.

CPD will continue to ensure that Brexit-related applications are progressed as efficiently as possible to enable it to have further firms authorised by 31 October. The main factors that will determine whether applications will be authorised by this date, are (a) the quality and timeliness of responses by applicants to comments issued, (b) the ability of applicants to identify/hire staff including those proposed to fulfil key roles and the subsequent completion of the fitness & probity assessment of PCF role holders, and in respect of the RI sector, (c) the volume of non-Brexit related applications. It should be noted that new Brexit-related applications continue to be received and it is anticipated that further Brexit-related applications will be submitted. Any future applications received are unlikely to be authorised by 31 October and the relevant firms will be so advised.

4.6. Registry of Credit Unions (RCU)

There are currently 243 active credit unions in Ireland with a total of 3.4 million members. As at 30 June 2019 the sector has total assets of €18.2bn, with €15.2bn in savings and €5bn of loans. The total realised reserves for the sector are €3bn (a 17 per cent sector average realised reserve ratio), up from €2.7bn in June 2017. Total regulatory reserves have also increased in this period from €1.8bn to €2.0bn, which indicates a strong overall reserves position for the sector.

At present no adverse trends are being reported by credit unions including in the border region, with no impact reported on liquidity or credit quality as ascertained from regulatory returns and direct engagement with credit unions. RCU has communicated our supervisory expectations with regard to Brexit planning by credit unions in recent editions of the ‘Credit Union News’ and other sector communications. We have been clear that credit unions should include any potential Brexit associated risks in their risk registers and ensure these risks are subject to regular monitoring and appropriate risk mitigants. We have reminded the sector that the range of risk considerations flowing from Brexit should remain an area for continual assessment by credit unions given the wider economic and financial impacts. It is expected that proactive contingency planning by credit unions, in particular regarding credit, savings, investments and IT security, is undertaken over the coming period in a no deal context.

No deal Brexit Impact on Credit Union Risk

The main no deal Brexit related risk to credit unions remains environmental and medium term in nature, stemming from macro-economic risks rather than cliff-edge effects. The impact of a no deal Brexit on the medium-term viability of credit unions remains unclear. Risks and commercial challenges in individual credit unions as a result of Brexit are likely to be particular to each credit union with some credit unions impacted more than others. This is dependent on the credit union's common bond, location, business model activities and characteristics of the local economy. RCU will continue to monitor the financial position of credit unions in assessing the impact a no deal Brexit may have on their medium-term viability.

Credit Risk

The principal impact that a no deal Brexit may have on all credit unions is that negative shocks to Ireland's economy reduce credit unions members' capacity to make loan repayments leading to an increase in defaults, loan arrears and write-offs. This may be hardest felt by credit unions with loan exposures to members employed in the agriculture, manufacturing, retail trade and tourism industries.

Investment Risk

The domestic focus of credit unions and the make-up of their investment portfolios (the majority of credit unions investments are in deposits in authorised credit institutions) limit immediate impacts that could arise from a no deal Brexit. However, present indications suggest that in the event of a no deal Brexit a number of financial institutions, based in the UK, with which credit unions hold some deposits and investments may return funds. This may pose a reinvestment risk to credit unions as finding suitable counterparties for these funds may be difficult, particularly if at short-notice and especially in a time of low or negative interest rates. A number of counterparties have indicated that they do not intend to return funds but RCU are awaiting confirmation from other counterparties. Where funds are not returned to credit unions they may not be compliant with the Central Bank's

Investment Regulations for credit unions.[9] RCU are giving consideration as to how transitional arrangements could be applied in such cases.

Operational Risk

[Omitted due to confidentiality]. For some credit unions, particularly those in the border region, a no deal Brexit could also impact the movement of staff living in Northern Ireland.

Border Region Credit Unions

42 community credit unions (with total assets of €2 billion and total membership of c.407,000) are operating in the counties along the border with Northern Ireland. The average total realised reserves ratio of these credit unions is 18 per cent – marginally higher than the sector average of 17 per cent. Given their location, the impact of a no deal Brexit may be more pronounced for them.

In March 2019, RCU Supervision Teams engaged directly with those 42 border credit unions to ascertain their level of Brexit awareness and preparedness. It was identified that those within closest proximity to the border were found to have a greater level of Brexit awareness and preparedness given the potential for increased cross border membership. No material or emerging risks specifically linked to Brexit were identified by the border credit unions during this exercise.

Current Actions

On 30 August, RCU issued a Brexit Questionnaire to all credit unions, including the border credit unions, seeking information on the level of Brexit preparedness, credit, investment and liquidity risks and operational risk, including cyber / IT.

To date, initial findings indicate no cliff edge effects. The Questionnaire responses are currently subject to further analysis and will inform RCU's supervisory actions over the medium term with regards to Brexit planning and monitoring, and will help to identify individual credit unions' lending and investment exposures most at risk from a no deal Brexit.

RCU has continued to communicate our supervisory expectations in relation to Brexit to all credit unions, including the importance of credit unions planning for the significant risks posed by a no deal

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[9] Under the Investment Regulations a credit institution is defined as *a person authorised as same pursuant to Directive 2013/36/EU*-credit unions are permitted to invest in accounts in credit institutions or bank bonds issued by credit institutions.

Brexit. This includes the 2019 Financial Year-End letter issued on 6 September and Credit Union Newsletter issued on 12 September.

4.7. Market Infrastructure

Practically all of the necessary actions have been completed to facilitate CREST – the securities settlement system operated by Euroclear UK and Ireland (EUI) to settle Irish corporate securities continuing to provide services in a no deal Brexit outcome. Conditional equivalence for the UK CSD framework and amendments to Irish Settlement Finality Directive (SFD) legislation and the Irish Uncertificated Regulations (USRs) [10] are now complete. The process for the Central Bank to conduct a technical equivalence assessment in order to advise the Minister for Finance in respect of systems seeking long term designation under the revised Irish Settlement Finality legislation has been agreed. Information relating to the notification and designation process for UK payments and securities settlements systems has been published on the Central Bank's website. The only action to be completed is a relatively minor change to the Companies Act by the Minister of Business Enterprise & Innovation (BEI). [Omitted due to confidentiality].

Long-term solution

Euroclear Bank continues to engage with the Irish market participants through its Working Group and Steering Board structures, as well as various bilateral meetings on the migration of the Irish market to Euroclear Bank in March 2021. The Irish authorities (Central Bank and Department of Finance) are represented on the Steering Board in an observer capacity. On 19 July it was announced that the Minister for Finance and Public Expenditure and Reform (PER) and the Minister for BEI had obtained Government agreement to draft legislation that could facilitate the longer term transition of the Irish securities market from its current settlement system to the industry selected settlement system operated by Euroclear Bank. The proposed legislation, when enacted, will provide an alternative mechanism, to Schemes of Arrangement under the Companies Act 2014, for issuers to migrate securities to the settlement system of Euroclear Bank Belgium. The outline of the future Migration of Participating Securities Bill was also published in July so as to facilitate market participant's engagement in the process.

[10] Companies Act, 1990 (Uncertified Securities) Regulations, 1996

5. Organisational Risk

Non-financial risks

The Organisational Risk Division (ORD) previously provided an update on the organisation wide assessment that was completed earlier in 2019. Contained below is an update on the status of that ongoing assessment. Originally, this process was envisaged as a three-stage assessment process with the first and second phase of the assessment heavily focused on engagement with first line divisions and the third phase being ongoing monitoring and challenge. ORD has now begun a fourth stage to ensure ongoing engagement with first line divisions to maintain the accuracy of the divisional risk registers around Brexit risk exposures as 31 October approaches, and to ensure that any new Brexit related risk exposures are identified and articulated.

Since the last update provided in June 2019, there has not been significant change to the Central Bank's operational risk environment as a result of Brexit. The five high level themes initially identified remain relevant, as any risks that have been subsequently identified by divisions sit comfortably within one of these themes. As a recap, the five high level themes identified were as follows, (i.) volume of authorisations, (ii.) increased scope of supervisory requirements, (iii.) adequacy of resourcing and the consequent need to re-prioritise existing work demands, (iv.) continuity and enforceability of legal contracts, and finally, (v.) ensuring General Data Protection Regulation (GDPR) requirements are managed.

[Omitted due to confidentiality].

As the Brexit situation unfolds, divisions are requested to review the RAG status and associated controls related to these risks. [Omitted due to confidentiality].

[Omitted due to confidentiality].

ORD will continue to review progress in this regard and challenge in line with the Central Bank's ORM Framework. As additional information regarding the Brexit scenario becomes known ORD will prompt divisions to review their relevant risk exposures.

Financial risks

[Omitted due to confidentiality].

6. Authorisations Activity

6.1. Overview

[Omitted due to confidentiality].

6.2. Asset Management Supervision

[Omitted due to confidentiality].

6.3. Banking

[Omitted due to confidentiality].

6.4. Consumer Protection

[Omitted due to confidentiality].

6.5. Insurance

[Omitted due to confidentiality].

6.6. Securities and Markets Supervision

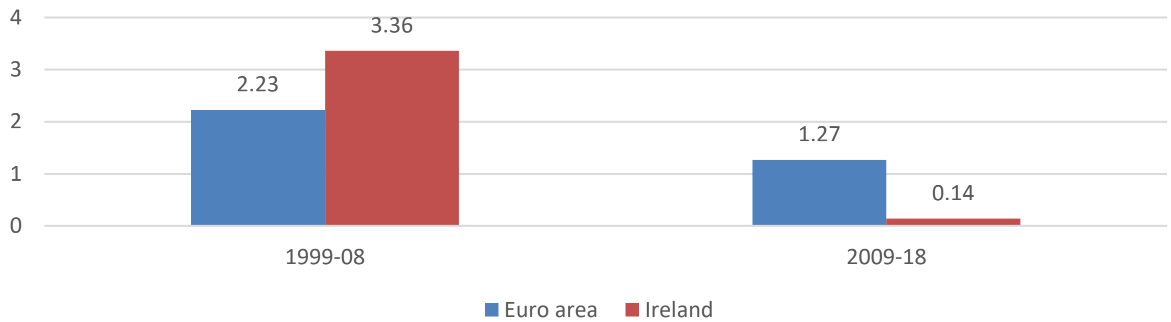
[Omitted due to confidentiality].

7. Special Topic 1: Grocery Prices in Ireland after Brexit[11]

The evidence we examine suggests that Irish consumers have typically experienced relatively high grocery prices over time. This is likely the result of a number of structural features of Ireland and its groceries market. In addition to short-term inflationary effects, a hard Brexit could exacerbate a number of these structural issues with potentially adverse consequences for consumers.

At different times, Ireland has experienced inflation differentials vis-à-vis the euro area average during its 20 years as a member of the single currency.[12] In the first decade of the euro, Ireland had consistently higher inflation than the rest of the euro area, particularly during the early 2000s (Chart 7.1). The reverse occurred in the following decade, with Irish inflation averaging about 1 per cent lower than the euro area average.

Chart 7.1: 20 Years of Inflation: Ireland and the Euro Area



Source: Eurostat

Despite fluctuations in relative inflation, the price level of groceries in Ireland, as proxied here by food and non-alcoholic beverage prices has remained persistently high. Ireland's food and non-alcoholic beverage prices were already above the euro area average when the currency was introduced in 1999. They then increased relatively rapidly during the first decade of the euro, and have declined somewhat in the crisis and post-crisis period (Chart 7.2). Yet, when one takes into account the level of expenditure per capita, food and non-alcoholic beverage prices appear to have been consistently high throughout the period relative to other Member States. There are a number of structural features of

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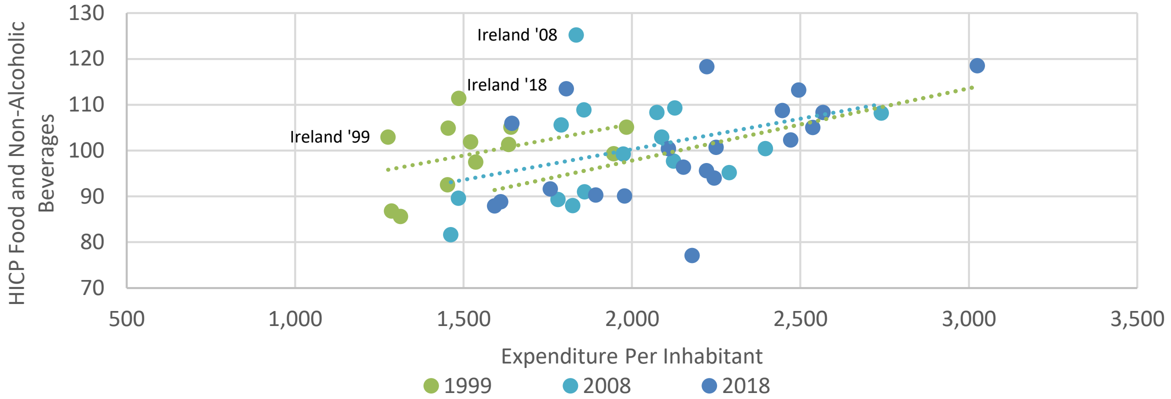
[11] Special Topic provided by David Horan, Peter McQuade, and John Scally (IEA).

[12] See for example: Honohan, P & Lane, P,R. (2003) "Divergent inflation rates in EMU," *Economic Policy*, CEPR;CES;MSH, vol. 18(37), pages 357-394, October.
Honohan, P. & Lane P,R., (2004) "Exchange Rates and Inflation Under EMU: An Update," CEPR Discussion Papers 4583, C.E.P.R. Discussion Papers.

Ireland, and the grocery market in particular, which may help to account for this pattern and which could be exacerbated by a hard Brexit.[13]

Chart 7.2: Groceries price level and expenditure: 1999, 2008, 2018[14]



Source: Eurostat
Note: 2015=100

As Ireland is a geographically remote country, Irish importers must pay relatively high transport costs compared to some other EU Member States. Chart 7.3 illustrates the average of trade costs estimated using a gravity model, and therefore reflect not only transport costs associated with distance, but also costs associated with linguistic, cultural or institutional barriers.[15] These data suggest that Ireland has relatively high trade costs, in common with other remote euro area Member States like Cyprus, Greece and Finland. A hard-Brexit may involve a change in the pattern of trade and transport to and from Ireland. The pink bars show the average estimated non-tariff shipping and trade costs, excluding goods imported from the UK, Ireland's closest trading partner. Having to import goods from more distant countries would lead to additional shipping costs for Ireland, while a diversion of trade via the UK would have a far more limited consequence for import costs in other Member States. However, trade costs are not the only potential factor contributing to Ireland's high grocery prices.

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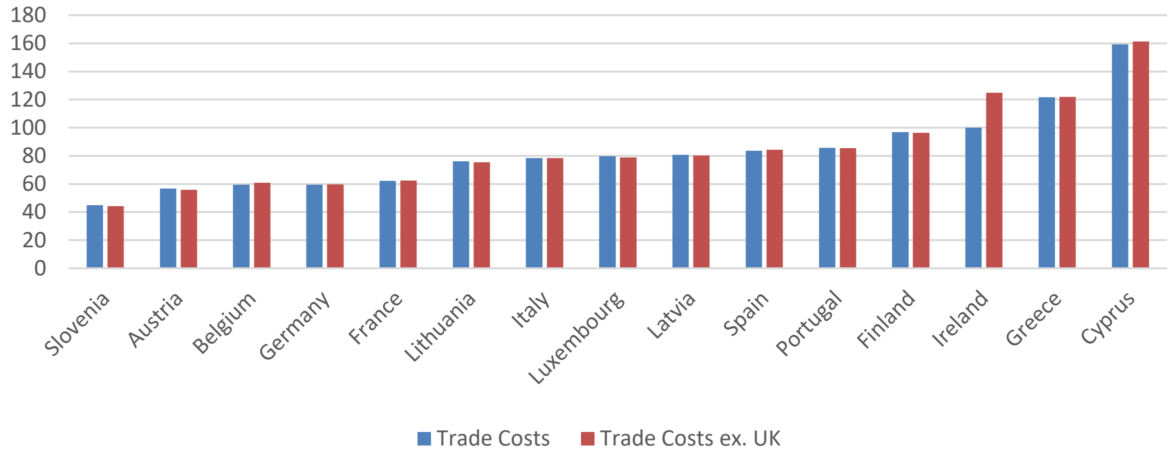
[13] See for example: ECB (2011) "Structural Features of Distributive Trade and their Impact on Prices in the Euro Area." Occasional Paper Series, No. 128.
ECB (2015) "Grocery Prices in the Euro Area: findings from the analysis of a disaggregated price dataset." European Central Bank Economic Bulletin 2015, No. 1.
[14] X-axis shows nominal expenditure per inhabitant (in euro) on food and non-alcoholic beverages. Y-axis displays an index of the price level of food and non-alcoholic beverages, where the EU15=100 for each year.
[15] Novy, Dennis (2013) "Gravity Redux: measuring international trade costs with panel data" Economic Inquiry, Vol 51(1).

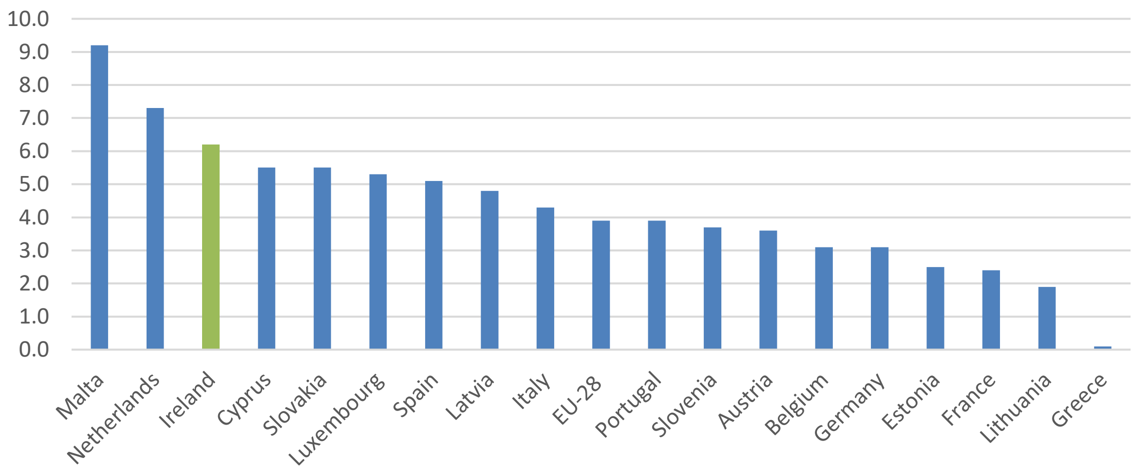
Chart 7.3: Trade/Shipping Costs



Source: Estimates based on ESCAP-World Bank Trade Cost Database, IMF direction of trade statistics and Central Bank of Ireland staff calculations. Note: Index of trade costs where Ireland=100

Proxy indicators suggest that grocery retail profits may be relatively high in Ireland. Of the countries for which data are available, only Malta and the Netherlands exhibit higher profitability in the groceries sector (Chart 7.4). Chart 7.5 suggests that this relatively high profitability compared to some other euro area Member States, such as Germany, has been a consistent feature for most of the past 20 years, with the exception of the period of the global financial crisis. While it is possible that this reflects higher mark-ups in Ireland, this indicator should be treated with caution as it could also be interpreted as showing a lack of efficiency in the German retail sector relative to Ireland.

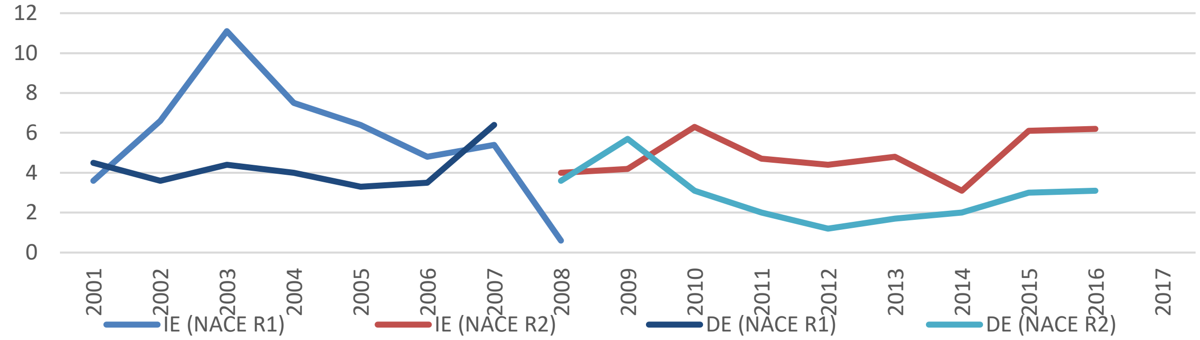
Chart 7.4: Profitability in Grocery Retail in the Euro Area (2016)[16]



Source: Eurostat

[16] Chart displays gross operating surplus/turnover in per cent for the category of retail sale in non-specialised stores with food, beverages or tobacco predominating.

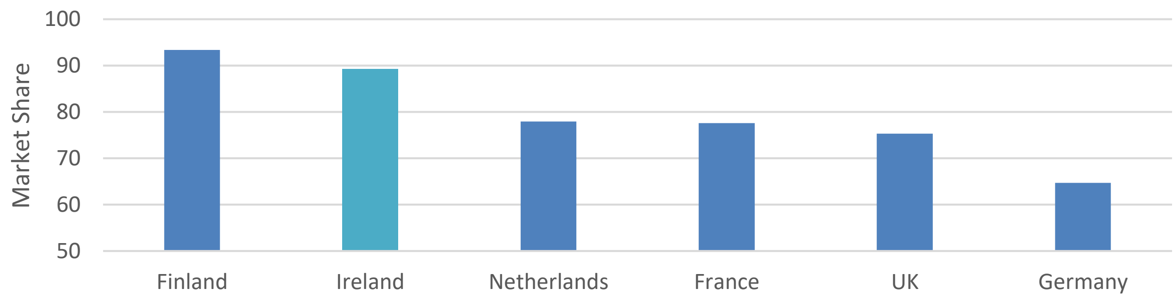
Chart 7.5: Profitability in Grocery Retail: Ireland vs. Germany 2001-2016[17]



Source: Eurostat Structural Business Statistics Note: Series report gross operating surplus/turnover in per cent for the category retail sale in non-specialised stores with food, beverages or tobacco predominating. Series discontinuity between NACE Revision 1 (R1), which ends in 2008, and NACE Revision 2 (R") which begins in 2008.

The top 5 grocery retailers in Ireland account for almost 90 per cent of the groceries market (Chart 7.6). In general, a higher degree of market concentration is expected to have a dampening effect on market competition, facilitating higher mark-ups and firm profitability. The concentration ratio in the Irish groceries market has increased since 2011, as a result of mergers in the sector.[18] For comparison, the equivalent concentration ratio is 75.3 per cent in the UK, 77.6 per cent in France, 77.9 per cent in the Netherlands. In contrast, at 93.4 per cent, the concentration ratio in Finland is even higher than in Ireland. It should also be noted that the distribution of market share among the top five retailers in Ireland is now more even compared to 2011, when the top two firms accounted for over half of the market. What is also notable is the increasing share of discount retailers, which rose from 9.1 per cent to 23.6 per cent over the period since 2011, and which may have contributed to competition and downward price pressures.

Chart 7.6: Grocery Market concentration in selected EU countries[19]



Source: Statistica, Kantar Worldpanel, Finnish Grocery Trade Association, Lebensmittelzeitung

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[17] Chart displays gross operating surplus/turnover in per cent for the category of retail sale in non-specialised stores with food, beverages or tobacco predominating. Series discontinuity between NACE Revision 1 (R1), which ends in 2008, and NACE Revision 2 (R2) beginning in 2008.
[18] Forfas (2011) "Review of the economic impact of the retail cap," Report prepared for the Departments of Enterprise, Jobs and Innovation and Environment, Community and Local Government, April 2011.
[19] Market share of top five grocery stores

UK grocery retailers maintain a significant presence in Ireland. In the context of Brexit, it is notable that a UK retailer had the third highest market share in July 2019, while other UK-based grocery retailers also maintain a significant presence in the Irish market.[20] Research has shown that anti-dumping tariffs on imports can lead to higher prices being charged by domestic firms, as reduced competition leads to greater market power for domestic firms.[21,22] However, the high profitability of the grocery retail sector may mitigate the likelihood of UK-based retailers leaving the Irish market, and thereby further increasing market concentration.

Increased tariffs and trade costs may be passed on to consumers. The market structure in the groceries market, if characterised as having low levels of competition and relatively high mark-ups, could imply that some of the increased trade costs associated with Brexit may be passed on to consumers, while the price of domestic substitute goods could also increase in the event of tariffs. Cole and Eckel (2018) demonstrate that traditional substitution effects – where consumers respond to higher prices on imports by substituting towards cheaper alternatives - can be dominated by retailers absorbing the additional costs of tariffs on imports through increasing their mark-ups on other more efficient, low cost products, where mark-ups tend to be highest.[23] Alternatively, high profitability could potentially allow retailers to absorb higher costs, lowering pass through to consumer prices. However, if retailers are forced to absorb Brexit related costs, they could respond by withdrawing less profitable products, leading to a reduction in variety with associated utility losses for consumers.[24] Overall, however, the relationship between UK and Irish producers, retailers and consumers is complex.

Imports from the UK are a substantial portion of the Irish groceries consumption basket. Chart 7.7 shows that agri-food products are the most exposed to high tariffs in a hard-Brexit scenario. Products in the milling industry, dairy products and meat products rely on imports from the UK, while the tariffs that would be applied to these goods, in the event of a no deal scenario, are sizeable. Lawless and Morgenroth (2018) examine the contribution of UK imports to overall household expenditure in Ireland and estimate their exposure to tariffs and other non-tariff related cost increases from possible

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[20] Source: https://www.statista.com/statistics/534106/grocery-market-share-ireland/

[21] An anti-dumping tariff is a protectionist tariff that a domestic government imposes on foreign imports that it believes are priced below market value.

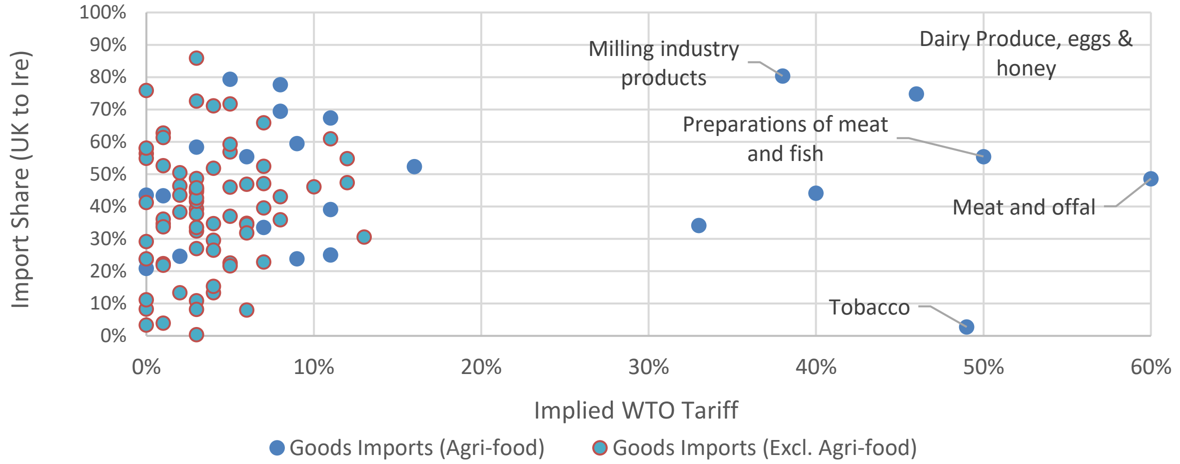
[22] Konings J. and Vandenbussche H. (2005) "Antidumping protection and markups of domestic firms", *Journal of International Economics,* Vol.65(1) p. 151-165.

[23] Cole, M.T. & Eckel, C. (2018) "Tariffs and markups in retailing," *Journal of International Economics*, vol. 113(C), p. 139-153.

[24] Cole, M.T. & Davies, R.B. (2014) "Royale with Cheese: Globalization, Tourism, and the Variety of Goods," *Review of Development Economics,* Wiley Blackwell, vol. 18(2), pages 386-400, May.

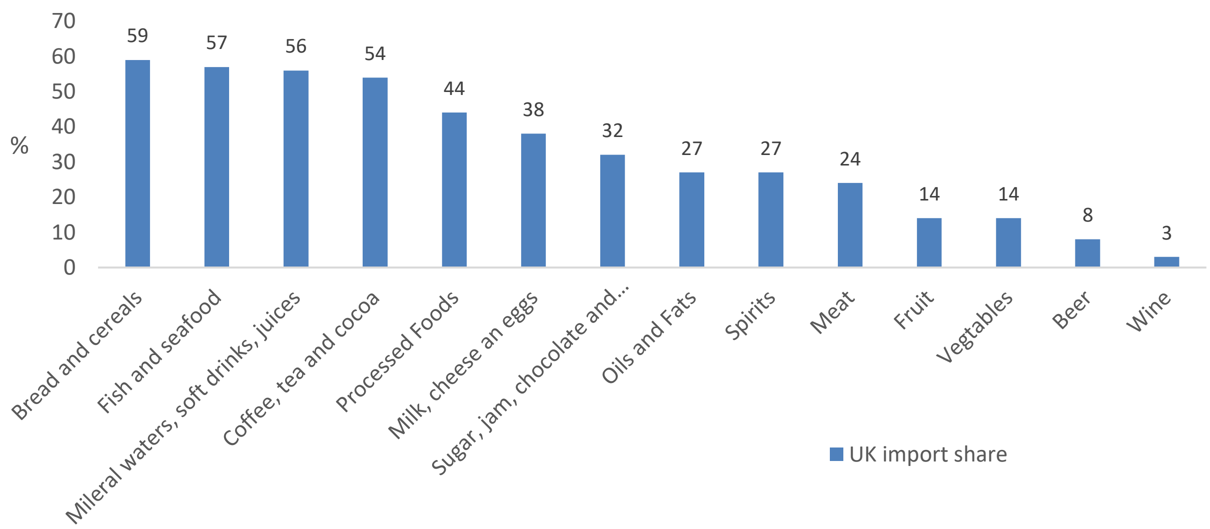
restrictions on trade.[25] The authors note that these are upper bound estimates of the potential price effects of a no deal Brexit as their study does not take account of possible exchange rate or substitution effects, and assumes full price pass through to consumers. Caveats aside, their estimates indicated that the sectors most exposed are bread and cereals, as 59 per cent of these products are imported from the UK. The dairy sector is found to have the highest potential sector-level price effect.

Chart 7.7: Concentration of Irish Imports from the UK and Implied WTO Tariffs[26]



Source: Lawless and Morgenroth (2018), Eurostat and authors' calculations.

Chart 7.8: UK Food Imports as a Share of Total Food Imports



Source: Lawless and Morgenroth (2018), Kee et al (2009)[27]

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[25] Lawless, M. & Morgenroth, E. (2018) "Brexit and Irish Consumers," Quarterly Economic Commentary: Special Articles, Economic and Social Research Institute (ESRI).

[26] Indicative values of average ad velorem equivalent tariffs estimated on the basis of the minimum tariffs weighted using EU imports from the UK at the HS 6-digit product level.

[27] Looi Kee, H., Nicita, A., & Olarreaga, M. (2008). Estimating trade restrictiveness indices. The Economic Journal, 119(534), 172-199.

A hard-Brexit could lead to some temporary increases in grocery inflation. Assuming no change in the exchange rate, full pass through of the tariffs and non-tariff barrier effects, and that consumers do not substitute away from UK products, the food price increases assumed by Lawless and Morgenroth (2018) would lead to an overall increase in the average basket of consumer goods. The *Processed Foods and Milk*, *Cheese and Eggs* categories make the largest contribution to the increases. In reality, these price increases are unlikely to fully materialise as consumers are likely to switch products, while producers may withdraw less profitable products from the Irish market. Moreover, weakening domestic demand and a sterling depreciation would exert downward pressure on Irish grocery prices. Nevertheless, some hard-Brexit related increase in the price level of groceries relative to other euro area Member States could prove to be persistent because of the potential adverse structural consequences described above.

Table 7.1: WTO and NTB Tariff Estimates

	WTO tariff rate %	Non-Tariff Barrier tariff equivalent estimates %	UK import share %
Bread and cereals	16	36	59
Fish and seafood	10	20	57
Mineral waters, soft drinks, juices	13	27	56
Coffee, tea and cocoa	7	29	54
Processed Foods	8	27	44
Milk, cheese and eggs	43	79	38
Sugar, jam, chocolate and confectionery	29	55	32
Oils and Fats	23	46	27
Spirits	7	9	27
Meat	38	62	24
Fruit	9	25	14
Vegetables	9	27	14
Beer	0	6	8
Wine	8	14	3

Source: Lawless and Morgenroth (2018), Kee et al (2009)

8. Special Topic 2: Short-term disruption to trade infrastructure in a no deal Brexit[28]

Much of the economic analysis conducted on the impacts of Brexit on the Irish economy has assessed the deviation from baseline GDP growth under various forms of the future trading relationship, i.e. a Free trade agreement; Customs Union, etc. In each of these scenarios, the status quo applies during a transition period lasting for one to two years.[29] This transition period means that firms, households and administrators are able to prepare for the move to a new trading arrangement between Ireland and the UK.

In a no deal/disorderly Brexit however, a transition period would not apply. This means there is not only the substantial impact of tariffs and non-tariff barriers, but substantial adjustment costs incurred as firms and administrative bodies in Ireland, the UK and other European countries would be required to implement all of the infrastructure, both administrative and physical, for trading with a third country in a very short period of time. This box analyses two of primary channels through which short term disruption may arise, logistical delays and the imposition of sanitary and phyto-sanitary (SPS) checks.

These effects mean that, in the case of no deal, the impact of Brexit on the forecasts is more severe in the short-term. This is primarily through their effect on trade, but also on domestic demand since a significant proportion of firms make use of intermediate inputs imported either from or through the UK.[30] Assessing the magnitude of this impact on output is difficult however. No country has ever left a free trade agreement with the level of integration that the UK has with EU member states. As such, we have used a significant element of judgement arising from economic theory and the best estimates available in the literature.

Logistics

A disorderly Brexit would mean that ports and logistics operators in Ireland, the UK and on the European continent would need to adapt to a substantial number of new regulations in a short space

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[28] Stephen Byrne, (IEA).

[29] The Bank has published a series of Quarterly Bulletin Boxes, for example (Conefrey, O'Reilly and Walsh, 2019). See also analysis by the Department of Finance and ESRI.

[30] See Martina Lawless (2018) "Intermediate Goods Inputs And The UK Content Of Irish Goods Exports". ESRI Working Papers

of time. In the long run, evidence suggests that these increases in delays and administrative burdens would reduce UK-Ireland trade by 9.6 per cent.[31]

In the short run, however, the process of adapting to new regulations and implementing a new tariff regime will result in delays at ports/airports compared with the status quo. Furthermore, there would likely need to be upgrades to port infrastructure to allow any delayed consignments to be stored, for traffic management, as well as to allow trucks to comply with tachograph rules, etc.[32]

As well as delays to Irish imports and exports to and from the UK, there may also be delays to Irish consignments travelling through the UK to the European market. While Irish trucks will still be able to transit through the UK using the 1975 TIR convention,[33] they will still be affected by any delays at UK ports. Furthermore, transiting under the TIR convention requires obtaining and paying for a permit[34] and will also require further administrative and learning costs, which are likely to be most acute in the months immediately following a disorderly Brexit.

Evidence suggests that Irish and UK firms engaged in significant stockpiling in advance of the 31 March 2019 deadline in order to mitigate the impact of the first months of adjustment in the event of a no deal.[35] An aggravating factor with regard to the October deadline is that it comes at a time in the year when warehouses are typically at peak capacity, meaning that stockpiling is more difficult and more costly.

These factors will hinder trade, potentially significantly, in the very short run, adding to the increase in input costs for Irish firms already incurred from tariffs and non-tariff barriers in late 2019 and early 2020.

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[31] Byrne, S. & Rice, J.(2018). Non-tariff barriers and goods trade: a Brexit impact analysis (No. 6/RT/18). Central Bank of Ireland.

[32] Seanad Committee on the Withdrawal of the United Kingdom from the European Union. Submission of the Freight Transport Association. 25th September 2019

[33] https://ec.europa.eu/taxation_customs/business/customs-procedures/what-is-customs-transit/tir-transports-internationaux-routiers-international-road-transport_en

[34] Currently TIR permits cost between $40 and $220 depending on the issuing country and other factors. See Morgenroth (2018)

[35] Bank of England (May 2019) Inflation Report

Sanitary and Phyto-sanitary (SPS) Checks

At present, animal, plant and non-animal food imports are subject to no checks at ports when arriving from the UK. When the UK becomes a third country, authorities at Ireland's ports will be required to implement EU SPS checks. The degree of checking required differs significantly for different goods and for different source destinations. For example, imports of food of animal origin from third countries are prohibited unless a number of regulations and certifications are acquired by both the third country and the exporting firm.[36] In a no deal, it is assumed that the UK will acquire the relevant certifications almost immediately, but there will likely be significant heterogeneity in the speed at which UK firms become compliant.

Importation of goods subject to SPS requirements may only occur through a designated first point of entry, currently Dublin port and Dublin airport. Each consignment undergoes documentary and identity checks, as well as physical checks at an "appropriate frequency". The frequency of physical checks is reduced on frequently traded items (more than 200 consignments per annum) according to a risk index maintained by the European Commission.[37]

Implementing these checks will require an increase in physical infrastructure at Ireland's ports (storage facilities, laboratory equipment for physical testing). Adapting to this new system in a short period of time in a no deal scenario will be problematic, and will likely result in further delays to trade significantly above what would be the case under a transition agreement scenario.

Mitigating factors

While the unprecedented and uncertain nature of a disorderly Brexit make it difficult to plan for, certain contingency measures have already been put in place that will mitigate the short run impact. The Government announced in 2018 that it would hire extra customs officials including additional staff to carry out checks on agricultural products.[38]

Revenue have also published figures which shows that 96 per cent of merchandise export trade with the UK in 2018 was carried out by firms which now have an "Economic Operators Registration and

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[36] See European Commission: Notice To Stakeholders Withdrawal Of The United Kingdom And EU Food Law And EU Rules On Quality Schemes
[37] https://ec.europa.eu/food/plant/plant_health_biosecurity/non_eu_trade/less_frequent_checks_en
[38] Parliamentary Question, 18th December 2018

Identification" (EORI) number, which is required by revenue for firms trading with a third country.[39] While having an EORI number does not reduce the impact of the factors discussed above, it implies that the majority of Irish firms who currently trade with the UK are aware of their requirements in the event of a no deal.

[39] Revenue press statement on Brexit engagement

Glossary

AIFM	Alternative Investment Fund Managers
AMAI	Asset Management: Authorisations and Inspections Division
AMLD	Anti-Money Laundering Division
AMIB	Asset Management and Investment Banking Directorate
AMS	Asset Management Supervision Directorate
BAML	Bank of America Merrill Lynch
BBI	Barclays Bank Ireland
BCG	Brexit Contact Group
BEI	Business Enterprise & Innovation
BIS	Bank of International Settlements
BISC	Brexit Insurance Supervisory Co-ordination Group
BoE	Bank of England
BoS	Board of Supervisors
BTF	Brexit Task Force
BSSD	Banking Supervision - Supervision Division
BSAD	Banking Supervision Analytics Division
CCP	Central Counterparty Clearing House
CPD	Consumer Protection Directorate
CSD	Central Securities Depository
CSDR	Central Securities Depositories Regulation
CSO	Central Statistics Office
DBEI	Department of Business Enterprise and Innovation
DoF	Department of Finance
EBA	European Banking Authority
EORI	Economic Operators Registration and Identification

ECB	European Central Bank
EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
EMI	Electronic Money Institutions
ESMA	European Securities and Markets Authority
ESRI	Economic and Social Research Institute
ETF	Exchange traded fund
EUI	Euroclear UK and Ireland
FCA	Financial Conduct Authority
FCR	Financial Crisis Response Protocol
FMD	Financial Markets Division
FMC	Fund Management Companies
FoE	Freedom of Establishment
FoS	Freedom of Services
FSC	Financial Stability Committee
FSD	Financial Stability Division
GDP	Gross Domestic Product
GDPR	General Data Protection Regulation
IEA	Irish Economic Analysis
INSA	Insurance - Actuarial, Analytics & Advisory Services
IR	International Relations
MiFID	Markets in Financial Instruments Directive
MiFIR	Markets in Financial Instruments Regulation
MoU	Memorandum of Understanding
MMoU	Multilateral Memorandum of Understanding
MPC	Monetary Policy Committee

MPD	Markets Policy Division
NAV	Net Asset Value
NCA	National Competent Authorities
ONS	Office for National Statistics
ORD	Organisational Risk Division
PI	Payment Institution
PMI	Purchasing Managers' Index
PRA	Prudential Regulation Authority
PSSD	Payment and Securities Settlement Division
RCU	Registry of Credit Unions
RI	Retail (insurance and mortgage credit) Intermediary
SCC	Standard Contract Clause
SCN	Supervisory Co-ordination Network
SFD	Settlement Finality Directive
SMSD	Securities Markets Supervision Division
SoR	Split of Responsibilities
SPE	Special Purpose Entity
SPS	Sanitary and Phyto-sanitary
SRD	Supervisory Risk Division
SSM	Single Supervisory Mechanism
TARGET	Trans-European Automated Real-time Gross settlement Express Transfer system
TPR	Temporary Permissions Regime
TRR	Temporary Run-Off Regime
UCITS	Undertakings for Collective Investment in Transferable Securities
USR	Irish Uncertificated Regulations
WTO	Word Trade Organisation