What would a Brexit transition deal actually mean for the UK economy?

Ahead of this week's EU summit, there has been a lot of talk about when a transition deal can be agreed. But it's not just a question of when, the details matter just as much

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With a transition deal, it's not just a question of when

When will a transition deal be agreed between the UK and EU? That's one of the big Brexit questions at the moment, and with the latest round of talks end in "deadlock", the consensus is, well, not soon.

The European Council is widely expected to vote at the end of this week that there has not been "sufficient progress" to justify moving talks forward. But a couple of weeks ago, there were reports that some countries were pushing to expand Barnier's mandate at this week's summit to allow a quick agreement on the transition deal, if not moving entirely on to discuss trade. That's looking less likely now - Germany and France are reported to be reluctant to progress without further commitments on the UK's financial liabilities.

Either way, the timing of the transition announcement matters because, with the clock ticking, firms are running out of time to enact contingency plans if they don't have certainty about the trading environment in the immediate Brexit aftermath - particularly given the renewed debate about a "no deal" scenario. Timing is also critical because the agreement should in principle see some delayed investment and hiring plans get enacted. But it's not quite that binary - the details count just as much as the announcement.

Here are four other factors that will affect how a transition period will affect the economy.

1 What actually is the transition deal?

This may sound like a fairly basic detail, but there has been some confusion in recent weeks over what the transition deal will entail. The UK government's official position is that an agreement will be fully negotiated and agreed by March 2019, with a transition - or rather implementation period - simply there for businesses to adjust.

But with the clock ticking on the article 50 process, there has been a lot of scepticism over whether it will be possible to agree on everything by March 2019. After this week, the next opportunity for the European Council to vote in favour of "sufficient progress" vote be in December. That would leave less than a year to negotiate the final deal, allowing in 4-5 months for ratification. Remember that CETA, the EU-Canada deal, took seven years to negotiate (although as many point out, the starting point between the UK and EU is obviously very different).

It is, therefore, possible that both sides agree to the framework of trade talks, perhaps with agreement on some "high level" principles, and leave the finer details to be thrashed out in the transition.

2 How long will the transition period be?

If that latter scenario does significant - and trade talks were to end up to continue in some form into the transition period - then the length will start to matter.

The UK is currently opting for a two-year transition, which could conceivably see the return of cliff-edge fears if there are many details about the post-Brexit trading environment left to be agreed. In the same way that businesses will need warning of the form the transition will take, they will also need to know what the UK's ultimate trading relationship will be well in advance of the transition coming to an end.

But it's not just firms who are uncertain. As was discussed in an interesting FT article today, there are many logistical considerations too when it comes to customs checks, and whether the two years would be enough to train the necessary staff and construct the required infrastructure to monitor the border.

3 What are the terms?

Following PM May's Florence speech, it looks increasingly likely that any transition phase would be "status quo". That means the UK will remain part of the single market during this time, which means businesses in theory only need to adjust once. But there is political disagreement on the role of the European Courts of Justice during the transition, given the UK would be subject to any ECJ rulings. And some UK politicians are against being a "rule taker" - where the UK must abide by the rules of the single market, but can no longer set them.

There have also been some questions raised by politicians on the European side as to what financial contributions the UK should make during the transition.

4 Will a transition deal be effective without clarity on a final deal?

This is a big question for the economy. The logic of a transition period is to avoid firms preparing for the worst case "cliff edge", but also to allow extra time to adjust to the post-Brexit environment. As we said earlier, that should see some shorter-term investment plans enacted. But given in all likelihood, the transition will be agreed before the details of the final trading arrangements; firms are likely to maintain an air of caution about their approach to more significant, longer-term investments in the UK.

All of this matters for the Bank of England

The Bank of England looks set to hike rates in November, but one of their key assumptions is that the Brexit process will be "smooth". But given the number of open questions, particularly on various Brexit issues, the Bank is likely to proceed cautiously until the picture becomes clearer. So at this stage, we feel it is more likely than not the Bank decides to stay hold through next year.

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