Association of International Retail

How the Figures Add Up. August 2025

1. Introduction

1.1 This is a short explanation of how AIR arrived at our figure of £5.65 billion additional spending and over 100,000 new jobs if the UK became the only large European country to offer VAT refunds to all international visitors on goods they buy in the UK and take home with them.

1.2 AIR does not have the expertise or resources of HMT and the OBR to undertake Treasury standard fiscal forecasting. Our aim is to demonstrate that there is a case to be made for HMT and the OBR to revisit the Treasury's 2020 forecast in light of new evidence and new data.

2. The 2020 HMT forecasts - background

2.1 It is important first to understand the forecasts that are currently being used by HMT to justify its decision not to reinstate tax-free shopping. The process below was outlined in detail in evidence to a Judicial Review and in two public briefing documents produced by HMRC ("VAT RES Technical Note" and" Mythbuster on the VAT Retail Export Scheme and tax-free airside sales").

2.2 As a member of the EU, the UK offered VAT refunds to non-EU international visitors. On leaving the EU, the Government had to treat all international visitors equally. This meant either extending tax-free shopping (the VAT Retail Export Scheme or VAT RES) to all EU visitors or ending it for non-EU visitors.

2.3 Ministers therefore first considered the cost of extending the VAT-RES to EU visitors. HMT forecast that the net cost of this would be £900 million pa. Ministers decided that this was not affordable and decided not to proceed with extending the scheme to EU visitors. As a result, by default, Britain ended tax-free shopping for non-EU visitors.

2.4 The Treasury forecast that the total cost to the Exchequer was £1.4 bn (£500m VAT refunded to non-EU visitors and £900m VAT refunded to EU visitors). This has subsequently been adjusted for inflation and the last public figure given as the cost by the Treasury was £2.5bn

2.5 These forecasts were made in mid-2020 when the Treasury was under great pressure, both because of the December 31st deadline for exiting the EU and because of the COVID-19 pandemic and lockdowns.

3. HMT estimate of the cost of extending the VAT-RES to EU visitors

3.1 This key HMT forecasts were made on the assumption that offering up to 20% discount would have little or no impact on the behaviour of international travellers, either in choosing to visit a country or on levels of spending.

3.2 To reach a net impact forecast, HMT combined the cost of introducing tax-free shopping for EU visitors (the deadweight cost of refunding VAT already paid) with the benefits in additional VAT gained by any increased visitor numbers and spending.

3.3 To calculate the maximum deadweight cost, HMT took the HMRC recorded level of VAT refunds to non-EU visitors in 2029 (£500 million) and multiplied it by 1.7, the ratio of non-

EU to EU visitors (1:1.7). This gave a figure of £900 million. Although this was stated as “up to £900 million”, it soon became the standard figure, not the extreme.

3.4 With the HMT assumption of “little or no impact on behaviour” extending the VAT RES was assumed to raise no additional VAT.

3.5 The gross £900 million cost for extending VAT RES to EU visitors therefore became the net cost.

3.6 The OBR has confirmed that it has never been asked to scrutinise this forecast.

4. <u>Why AIR believes the 2020 forecast needs to be reviewed</u>

4.1 AIR believes that the evidence does not support this forecast.

4.2 First because the data shows that the deadweight cost of extending the VAT RES to EU visitors was £50 million, not £900 million. Stores sales records show that EU shoppers accounted for only 10% of all international sales in 2019, suggesting that VAT was 10% of £500 million, not 170% of it.

4.3 This is because shop prices in the UK and EU are similar so there is no incentive to shop excessively. In contrast, non-EU visitors were responding to the incentive of up to 20% off.

4.4 Secondly, the evidence of British travellers, able to shop tax-free in the EU since 2021, demonstrates that offering VAT refunds does have a significant impact on international visitor behaviour. HMT’s assumption was that it would not.

4.5 In 2024, Brits spent £730 million on tax-free shopping in the EU, up from £125 million in 2021. It is likely to rise to £1 billion in 2025. Importantly, bed nights in Paris doubled for British visitors (2019-2023) while remaining virtually static for other European visitors. So, this is a new market of shopping-led tourists, spending additional money on accommodation, food, travel, leisure and culture, on all of which they pay VAT.

4.6 Based on this evidence, AIR estimates that instead of a £900 million cost to the Exchequer, introducing the VAT RES for EU visitors would create a new EU shopping-led market of at least £3.65bn annually, generating around £500 million net addition VAT and creating 73,000 new jobs.

5. <u>How AIR reached its £3.65 billion EU market forecast</u>

5.1 AIR’s forecast is based on evidence of actual spending patterns. We have deliberately chosen to focus on the lower end of forecast spectrum.

- Fact one: in 2024, British visitors spent £730 million on tax-free shopping in the EU[1]
- Fact two: this was mainly a new market, not just the same visitors spending more[2]
- Fact three: in 2019 non-EU visitors spent 6 times more on VAT-able goods and services than on tax-free shopping (£15 bn: £2.5bn)[3]
- Fact four: there are 66.7 million UK citizens and 448 million EU citizens (1: 6.7)

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[1] Industry data on actual VAT refund claims

[2] For example, Paris tourist office state that in 2023 bed nights for British visitors was over 230 % of 2019 levels, whereas it stayed largely stable for other European visitors

[3] VisitBritain spending data and HMRC VAT refund data

- Fact five: EU shopping VAT deadweight is just £50 million[4]

5.2 The AIR estimate is deliberately conservative. It assumes:

- EU visitors would spend only the same amount as UK visitors i.e. £730 million, not 6.7 times a much
- EU visitors would spend on shopping and other goods and services at a ratio of just 1:4, not 1:6 (to allow for the fact that these would be shopping-led trips)

5.3 This results in:

- EU spending on tax-free shopping: £730 million
- EU spending on associated goods and services: £2.92 billion
- **Total EU spending is £3.65 bn**
- **Spending in the regions: £1.8 billion**[5]
- Gross VAT would be £584 million
- **Net VAT, minus £50 million deadweight, £534 million**

6. <u>An alternative spending scenario</u>

6.1 The AIR estimate in Section 5 is a conservative figure to demonstrate the potential new market. There is an alternative scenario which AIR believes is more likely.

6.2 Assume EU residents (6.7 times larger than UK) spend just three times as much as British: £2.19 billion.

- **EU spending on associated goods and services: £8.76 billion**
- **Total EU spending would be £10.95 billion**
- Gross VAT would be £1.75 billion
- **Net VAT, minus deadweight, £1.7 billion**

7. <u>An alternative tax raising scenario</u>

7.1 HMT's forecast only look at the direct fiscal impact on VAT. But there is also a wider, indirect Exchequer impact (additional income tax, NI, Corporation Tax, VAT and reduced unemployment costs). Economic modelling suggests that for every £1 spent by an international visitor, the total gain for HMT is 37p[6]

- **This would suggest that in AIR's standard forecast, the Exchequer would gain £1.35 billion**
- **In AIR's alternative spending scenario, the Exchequer would gain £4 billion**

8. <u>The non-EU market</u>

8.1 Having decided not to extend the VAT RES to EU visitors in 2020, the Government had to end the existing system for non-EU visitors. HMT forecast the impact of this on the Exchequer.

8.2 HMT again made the assumption that removing the up to 20% discount would have little or no impact on the behaviour of international travellers, either in choosing to visit a country or on levels of spending.

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[5] VisitBritian figures show that 51% of EU visitors spending is in the regions
[6] Standard ratio used by economists e.g. Oxford Economics

8.3 HMRC estimate that in 2019, non-EU visitors reclaimed £500 million of VAT. Officials presented a forecast to minister that estimated a £500 million net gain to the Exchequer in VAT, assuming no reduction is spending levels and little or no fall in visitor numbers.

8.4 After the decision had been made, the OBR scrutinised the forecast for non-EU visitors only. It disagreed with the Treasury's assumption and, using a price elasticity of 1.9, reduced the forecast VAT benefit by 26% to £370 million. HMT adjusted its forecast accordingly.

8.5 Evidence presented by AIR to HMT in November 2023, based on actual spending figures, showed that spending had fallen by 25% in 2022 compared with 2019 levels.[7]

8.6 However, this was in the context that non-EU international visitor spending in EU states in 2022 had increased by 50% on 2019 levels. AIR suggested that, if Britain had still offered tax-free shopping, its share of this growth would have been an additional £1.5bn. This meant that the decline in spending levels in the UK, taking account of the growth, was around 50% on 2019 levels.

8.7 Evidence of non-EU spending on shopping in 2024 shows that the UK has plateaued at around 75% of 2019 spending levels while across the EU the average is 158% of 2019 spending levels. **This suggests a loss of £2bn in spending for the UK.**

9. <u>Combined figures</u>

9.1 Using its conservative assumptions, creating the new EU shopping-led tourism market and winning back the non-EU spending from continental rivals, **AIR estimates would give a combined value of £5.65 billion**

9.2 Using the British Retail Consortium ratio of jobs supported by spending levels (one job per £50,000 spending), this suggests **a total of 113,000 new jobs created**.

9.3 Using the standard return to the Exchequer of 37p per pound spent, this would suggest a **benefit to the Exchequer of just over £2 billion**.

9.4 These are based on the conservative estimate of EU spending levels and could be significantly higher.

10. <u>Distribution of Growth</u>

10.1 The previous government stated that, because 80% of tax-free shopping took place in London, there was little benefit for the regions. Industry pointed out that £500 million was still spent on tax-free shopping in the regions. Industry also showed how British brands used London as their global shop window and that tax-free shopping sales supported manufacturing jobs throughout the UK, for example in Scotland, the Midlands and the South West. The closure of Mulberry's London store was proof of this relationship.

10.1 But the requirement to offer tax-free shopping to EU visitors, creating a new 450 million market, estimated to be worth at least £3.65 of additional spending, would benefit the whole of the UK. VisitBritain states that currently around half of all EU visitor spending takes place outside London. This would be worth £1.8bn on top of the £500 million spent by visitors from the rest of the world. Regional airports, why mostly fly to EU destinations, would get an additional boost, both in passenger numbers and tax-free sales.

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[7] AIR Impact Study presented to HMT 2023. Available on the AIR website