Brexit: Potential Implications for the Irish Agri-food Sector

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Outline

• The terms of Brexit
  – Trade policy
  – UK Ag policy
• Current trade relations between
  – UK and EU
  – IRL and UK
• Implications of Brexit for EU
• Implications of Brexit for Ireland’s agri-food exports
• Uncertainties ….. And there are many!

So many unknowns

• Brexit is a step into the unknown
• Vote to Remain: Relatively known outcome
  – No impact on future trade
• Vote to Leave: Completely unknown outcome
  – No indication of UK’s trade relationship with the world
  – No indication as to what UK ag policy would be
• A comprehensive analysis of Brexit cannot therefore be produced at this time
• But we can provide an assessment of the consequences based on a set of Brexit assumptions
Mechanics of Brexit

• Brexit Vote June 23rd
• If UK votes to Leave then what happens next?
  a) Nothing (paralysis)/ stalling for time?
  b) Further renegotiation and another referendum?
  c) Brussels immediately notified of intention to leave?
• Clock starts ticking once intention to leave is notified
  – prompts a two year negotiation process on exit terms
  – which could be extended with consent of EU
  – preferable for UK to leave on amicable negotiated terms
  – but possible that UK might exit with no trade terms in place

Exit Dates?

• At the very earliest mid 2018
  – But could be messy as MFF revisions would be required
• Possibly 2020
  – Neater solution as it marks end of current MFF period
• Probably some time after 2020
  – The complexities of Brexit make a later departure more practical than an early one
• However, Eurosceptics may apply pressure for Brexit to occur as soon as possible
  – to ensure it occurs within life of current UK government
What will Brexit require?

• Negotiation of trade relations between EU27 and UK
  – UK application for WTO membership
• Negotiation of trade relations between UK and other WTO members
• Resolution of tariff levels and TRQs
• Past experience shows that trade negotiations are very time consuming
• Concern that UK may lack professional capacity
  – Given that UK trade matters have been dealt with by EU since 1973

Brexit Trade Terms

• Decision required on trade relationship with EU
• Agriculture might be included/excluded from any trade agreement with EU
• Could result in all manner of trade relationships e.g.
  a) No tariffs on EU UK trade
  • i.e. free trade between UK and EU
  b) MFN tariffs
  • UK and EU treat each other as WTO members
  c) Unilateral UK tariff reduction
  • Lopsided outcome where UK faces tariffs on its exports to EU but reduces or removes tariffs on imports from EU and other WTO members
• Questions also about what sort of TRQs the UK could establish
  – May not be able to acquire a pro rata share of existing EU TRQs
  – Subdivided UK/EU TRQ limits are less valuable to 3rd country exporters
Suite of Brexit Trade Terms

• 11 possible trade relationship outcomes for agriculture

<table>
<thead>
<tr>
<th>The UK’s relationship with the EU</th>
<th>Agriculture ‘in’ an agreement</th>
<th>Agriculture ‘out’</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Existing most-favoured-nation (MFN) tariffs</td>
<td>Unilateral tariff reduction by the UK</td>
</tr>
<tr>
<td>Customs Union</td>
<td>1</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>European Economic Area</td>
<td>4</td>
<td>5</td>
<td>6</td>
</tr>
<tr>
<td>Simple Free Trade Area (FTA)</td>
<td>7</td>
<td>8</td>
<td>9</td>
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<tr>
<td>No formal link</td>
<td>10</td>
<td>11</td>
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</tbody>
</table>

Source: Swinbank (2016)

Brexit Trade Terms?

• Some outcomes more likely than others
• Full UK trade liberalisation in agriculture is unlikely
• Tariff elimination would expose UK dairy and drystock
  – Severe competition from low cost non EU exporters
• UK likely to see dairy and drystock as “sensitive products”
  – Offering only limited or no tariff reductions for these sectors
And to compound matters…. need to decide UK Ag Policy

- UK would also be free to set agricultural policy
- Reform of UK ag policy is likely to be gradual
- In short term
  - Likely that this would be closely aligned to the CAP
  - This would be less disruptive to UK agri-food sector
- In medium term
  - Direct payments unlikely to pass a UK Treasury value for money audit
  - Likely to see a movement away from income support direct payments
  - Progression towards smaller ag payment budget, geared towards environmental considerations

Brexit Implications for CAP
Loss of the UK Budget contribution

Source: Matthews (2016)
What will Brexit mean for Irish Trade?

• The good news
  – Agri-food trade will not cease
  – The UK is too dependent on imports and will not embark on a food self-sufficiency policy

• The bad news
  – Irish exports will face more competition in UK
  – Trade from Ireland will be impeded and
  – Trade will be diverted from UK to other markets

What is trade diversion?

• Simply put, trade diversion is a change in export destination
• It is usually caused by a change in tariffs or other trade costs
  – Which affect the competitiveness of exports
• Country B (Britain) leaves a customs union (EU)
• Exports from country I (Ireland) to country B are reduced
  – Country B import more from country Z (e.g. New Zealand)
  – Country I exports more to country F and country G (EU Member States)
• Trade diversion has a negative outcome for exporting country (I)
  – Prices may be lower in the country that trade is diverted to
  – Transportation and other logistical costs may also be higher
  – Additional costs associated with market development
UK Agri-Food Trade

- Second largest economy in EU28
- UK is a major net importer of food
  - Unlike most other large EU member states
- UK has an agri-food trade deficit of €27.6 billion (2014)
  - This trade deficit is mainly with the EU
- UK self-sufficiency higher in some agri-food sectors
  - Net imports of dairy, beef, pig meat, fruit are significant
  - Relatively balanced trade position for cereals & sheep meat
  - Large positive net exporter in beverages

Who are the UK’s major agri-food import suppliers

- Main exporters of agri-food to the UK
  - Netherlands, Spain, France, Germany and Ireland
- Beef
  - Ireland
- Dairy
  - Ireland
- Sheep meat
  - NZ and Australia
- Pig meat
  - Denmark, Netherlands, Germany
- Fruit and Veg
  - Netherlands and Mediterranean Member States
UK Fresh Beef Imports (Volume) -2014

Source: Eurostat COMEXT

UK Sheep Meat Supply & Use Balance (2001-2014)

Source: DEFRA (2015)
UK Sheep Meat Imports (volume) - 2014

Source: Eurostat COMEXT

UK Sheep Meat Exports (volume) - 2014

Source: Eurostat COMEXT
UK Butter Imports (volume) - 2014

Source: Eurostat COMEXT

UK Cheese Imports (volume) - 2014

Source: Eurostat COMEXT
Ireland Merchandise Exports (1999-2015)

Source: Eurostat COMEXT

Ireland Merchandise Imports (1999-2015)

Source: Eurostat COMEXT
Irish Agri-Food Exports by Destination (1999-2015)

Source: Eurostat COMEXT

Irish Agri-Food Imports by Source (1999-2015)

Source: Eurostat COMEXT
Irish Agri-Food Exports by HS2 Chapter and Share of Chapter to UK (2014)

Key Brexit Assumptions

- The UK leaves the EU
- The UK joins WTO
- The CAP remains unchanged
- No new trade deals are entered into by the EU
- UK agricultural policy mimics the CAP
  - at least for a transitional period

Source: Eurostat COMEXT

The Irish Agriculture and Food Development Authority
Brexit Scenarios

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Share of Irish-UK exports that are diverted (%)</th>
<th>Reduction in value of diverted trade (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core Scenario 1</td>
<td>21.5%</td>
<td>-15%</td>
</tr>
<tr>
<td>Scenario 2</td>
<td>56.6%</td>
<td>-15%</td>
</tr>
<tr>
<td>Scenario 3</td>
<td>21.5%</td>
<td>-30%</td>
</tr>
<tr>
<td>Scenario 4</td>
<td>56.6%</td>
<td>-30%</td>
</tr>
</tbody>
</table>

Impact of Brexit on the Value of Irish Agri-Food Trade (I)

<table>
<thead>
<tr>
<th></th>
<th>Share of UK trade diverted (%)</th>
<th>Reduction in value of diverted trade (%)</th>
<th>Value of Exports in 2014</th>
<th>Value of Exports Under Brexit</th>
<th>Change in Value of Exports</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core Scenario 1</td>
<td></td>
<td></td>
<td>€ billion</td>
<td>€ billion</td>
<td>€ billion</td>
<td>percentage</td>
</tr>
<tr>
<td>ESRI/Hufbauer and Schott estimate &amp; assumed 15% reduction in value of diverted trade</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>UK</td>
<td>21.5</td>
<td>-15</td>
<td>4.52</td>
<td>3.55</td>
<td>-0.97</td>
<td>-21.5</td>
</tr>
<tr>
<td>Other EU</td>
<td>21.5</td>
<td>-15</td>
<td>3.28</td>
<td>4.10</td>
<td>+0.83</td>
<td>+24.5</td>
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<tr>
<td>Rest of World</td>
<td>21.5</td>
<td>-15</td>
<td>2.85</td>
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<td>0</td>
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<tr>
<td>Total</td>
<td>10.65</td>
<td>10.50</td>
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<td>-0.15</td>
<td>-1.4%</td>
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</table>

Alternative Scenario 2: Larger Trade Diversion based on Hufbauer and Schott estimate for agri-food trade & assumed 15% reduction in value of diverted trade

<table>
<thead>
<tr>
<th></th>
<th>Share of UK trade diverted (%)</th>
<th>Reduction in value of diverted trade (%)</th>
<th>Value of Exports in 2014</th>
<th>Value of Exports Under Brexit</th>
<th>Change in Value of Exports</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK</td>
<td>56.6</td>
<td>-15</td>
<td>4.52</td>
<td>1.96</td>
<td>-2.56</td>
<td>-56.6%</td>
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<tr>
<td>Other EU</td>
<td>56.6</td>
<td>-15</td>
<td>3.28</td>
<td>5.45</td>
<td>2.18</td>
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<td>Rest of World</td>
<td>56.6</td>
<td>-15</td>
<td>2.85</td>
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<tr>
<td>Total</td>
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<td>10.26</td>
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<td>-0.38</td>
<td>-3.61%</td>
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Source: Authors’ Calculations
Impact of Brexit on the Value of Irish Agri-Food Trade (2)

<table>
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<tr>
<th>Share of UK trade diverted (%)</th>
<th>Reduction in value of diverted trade (%)</th>
<th>Value of Exports in 2014</th>
<th>Value of Exports Under Brexit</th>
<th>Change in Value of Exports</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alternative Scenario 3: Trade diversion based on ESRI/Hufbauer and Schott estimate and assumed 30% reduction in value of diverted trade</td>
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<tr>
<td>UK</td>
<td>21.5</td>
<td>4.52</td>
<td>3.55</td>
<td>-0.97</td>
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<tr>
<td>Other EU</td>
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<td>3.28</td>
<td>3.96</td>
<td>0.68</td>
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<td>Rest of World</td>
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<td>2.85</td>
<td>0.00</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total</td>
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<td>10.65</td>
<td>10.35</td>
<td>-0.29</td>
<td>-2.74%</td>
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<td>Alternative Scenario 4: Larger Trade Diversion based on Hufbauer and Schott estimate for agri-food trade &amp; assumed 30% reduction in value of diverted trade</td>
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</tr>
<tr>
<td>UK</td>
<td>56.6</td>
<td>4.52</td>
<td>1.96</td>
<td>-2.56</td>
<td>-56.6%</td>
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<tr>
<td>Other EU</td>
<td>56.6</td>
<td>3.28</td>
<td>5.07</td>
<td>1.79</td>
<td>54.7%</td>
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<tr>
<td>Rest of World</td>
<td>56.6</td>
<td>2.85</td>
<td>2.85</td>
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<td>0.0%</td>
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<tr>
<td>Total</td>
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<td>10.65</td>
<td>9.88</td>
<td>-0.77</td>
<td>-7.22%</td>
</tr>
</tbody>
</table>

Source: Authors’ Calculations

What about UK agri-food exports to Ireland?

- We have not focused on Brexit impact on agri-food imports
  - 2014 imports of €4.1 bn vs exports of €4.5 bn
- If Brexit reduces UK agri-food exports to Ireland
  - Opportunities for Irish indigenous producers to fill gap in market
  - Alternatively, products could be sourced from elsewhere in the EU27
- Outcome would depend on
  - Capacity of indigenous Irish food producers to scale up production
  - Decisions by Irish retailers to use non UK suppliers, and
  - Irish consumer preferences for Irish products vs EU27 products
- Some Irish agri-food businesses could benefit from Brexit
  - Particularly those with limited exposure to the UK market
  - Brexit could lead due to reduced competition on the Irish market
Caveats and uncertainties

- Post Brexit UK Agri-food policy is unknown
  - Agri-food
  - Trade
- TRQ and Preferential Trade access post Brexit
- Macroeconomic uncertainty and impact of Brexit
  - Exchange rates, competitiveness and GDP growth
- Trade liberalisation and sensitive products
- All island agri-food processing sector integration
- Consumer preferences for food products – where will Irish consumers get their Kit Kat?

Brexit Conclusions (1)

- Outcome of vote and economic impact highly uncertain
- Post Brexit, UK unlikely to pursue agri-food self-sufficiency
  - Since the Corn Laws the UK has relied on trade
  - No reason to expect volte face
- Reason to expect UK to shy away from unilateral free trade
  - UK recognises that it may be vulnerable in livestock sectors
  - Sensitive product status for livestock sectors?
- Not credible to imagine agri-food trade between UK and Ireland coming to a stop
- Other Irish agri-food export markets now much more important than historically
  - Dilutes the trade impact of Brexit somewhat
Brexit Conclusions (2)

- Brexit likely to involve at least some additional trade barriers between UK and Ireland
  - Exports from Ireland to UK likely to be reduced
  - Exports diverted to other lower value markets
- Overall Irish agri-food export value reduced
- Export value to non-UK destinations likely to increase
- Magnitude of trade diversion and loss of export value uncertain
  - Trade and ag. policy dependent

Brexit Conclusions (3)

- Core Scenario:
  - Trade diversion based on ESRI analysis
  - Augmented by reduction in value of diverted trade
- Three alternative scenarios
  - Greater diversion of trade
  - Larger reduction in value of diverted trade
- In Core scenario Irish agri-food exports reduced
  - €150 mn per annum (-1.4%)
- Most negative alternative scenario
  - Close to €800 mn per annum (-7.2%)
Brexit Conclusions (4)

• Exposure to UK market is not uniform
  – varies by agri-food product and commodity category
  – Varies by agri-food firm
  – Certain industry/firm specific risks from Brexit likely to be higher

• If the UK votes “leave”
  – Need for further detailed analysis of the impact on Irish agriculture and agri-food industry

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