

# **Which British agricultural product could be a competitive in EU market after Brexit?<sup>1</sup>**

## **Introduction**

Uncertainty is the only certainty. We can say in the case of Brexit too. But what is Brexit? As a result of a longer preparation process, 51.9 percent of voters voted in the United Kingdom on 23 June 2016 in the form of a referendum to leave the European Union. (BBC, 2016) On March 27, 2017, Tim Barrow, Ambassador of the United Kingdom of Great Britain issued a letter of formal withdrawal to Donald Tusk, President of the European Council. Thus, the negotiation process on exit has begun, but the conditions for the United Kingdom's withdrawal from the EU (Brexit) are not yet known at the finishing of this paper. After the announcement, it was almost a year before the European Commission presented on 19 March 2018 the draft agreement about the exit. (EC, 2019b) As things stand, the United Kingdom (UK) is due to leave the European Union at 23:00 GMT on 31 October 2019.<sup>2</sup> But this could be changed. Negotiations between the EU and UK and the related UK decision-making mechanism have caused major problems in the adoption of the exit agreement. Significant political tensions in the process include the evidence that British Prime Minister Theresa May resigned on Friday, May 24, that she will leave the government and the Conservative Party on 7 June. (BBC, 2019) Until the finishing of this manuscript, it was not clear who would take over her position and in what direction he/she wanted to continue the negotiations. However, it is already clear that the EU does not want to renegotiate an agreement that has already been concluded and it will have a significant impact on EU and UK as well. At present, this process can be completed in a few ways, and it is possible to present more alternatives to exit conditions. But there is a great chance that the EU will consider the United Kingdom as a third-party WTO member and as a result will apply customs duties.

## **Literature overview, theoretical background**

It is clear too, that the Brexit will be caused significant macroeconomic difficulties. (e.g. Halmai, 2018; KPMG, 2017) Almost all sectors will be affected by exit, but the consequences vary. The role of the agri-food sector is specific, because the United Kingdom can only produce 61% of its needs. The EU is one of the UK's most important trading partners. Several studies have also examined the commercial effects of Brexit. (e.g. House of Lords, 2017) But it is worth examining to what extent British exports to the EU can change and what impacts can be prepared? Within this framework, the overall aim of the United Kingdom's foreign trade situation and the sectoral features of the agri-food industry, including the mainstreaming of agricultural trade, is to be found. Therefore, the main commercial processes, trends in individual products and the main outlook are reviewed. In order to present foreign trade processes, the trade data of the European Union Statistical Office, EUROSTAT will be presented. During the examination, competitive calculations under the current circumstances will be carried out.

The events of 2019 are greatly influenced by the fact that the Brexit referendum has resulted in a protracted period of instability. After the decision on Brexit, the UK will have to negotiate exit conditions and a new relationship with the EU. At the same time, it must renegotiate trade agreements with several other countries or apply general WTO rules. Resolving these issues can take years. Uncertainty and unfavourable outlooks can make investment and economic expectations a long time. In the long run, significant losses are expected. Increased restrictions reduce migration,

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<sup>2</sup> At the special summit on 10 April in 2019 EU leaders agreed an extension of Article 50 until the end of October 2019. If the withdrawal agreement is ratified by both sides earlier, the UK will leave on the first day of the following month. (European Council, 2019)

investment and productivity, resulting in increased trade, foreign direct investment, and increased labour supply. The broad range of estimated losses reflects the assumptions made by the UK on possible future economic relations with the EU and the rest of the world. Even today, the question of whether a soft or hard Brexit scenario applies to Britain is still a crucial issue<sup>3</sup>. Although the UK government wants hard Brexit in the first place, without the lack of a political agreement, this version can only calculate with conditionally. The (hard) Brexit argued - among others - that:

- Eliminate unnecessary regulations. This would place a huge burden on British businesses, which could become more effective;
- Britain could enter into better trade contracts than the EU, and commercial policy conditions for British companies could improve on the world market;
- The British Government would be free to decide who would be allowed to enter and who would reduce social-cultural tensions and lead to more balanced labor market conditions;
- Britain would get rid of the net contributor position of the common budget. (Halmai, 2018)

Although the probability of hard Brexit is very high. The most serious version is the possibility of a complete exit from the EU Member States without any agreement on all relevant issues (no deal). What happens to customs when the UK exits the EU? The United Kingdom can reduce its import duties on third countries while, in the absence of negotiated agreements, export duties and non-tariff barriers are increasing. If the United Kingdom enters the WTO system independently, it can reduce the import duties set by the EU Customs Union (Common Customs Tariff)<sup>4</sup>.

The situation is similar for the EU: if there is no agreement with the EU, UK exports to the EU are subject to EU standard MFN duties. British companies exporting to the EU, and since the UK is no longer a member of the EU Customs Union, face higher administrative costs and higher non-tariff barriers.

## Material and methods

During the presentation of bilateral relations, I used the trade database of the European Union Statistical Office. Prior to presenting the results, the following should be underlined: for country data, the breakdown by sector and product range is based on the trade values available in the SITC (Standard International Trade Classification) and the Harmonized System (HS). (Eurostat, 2019)

For some commodities, the EU should be accepted as a condition for trade in goods between the UK and the EU: values do not, in many cases, indicate that the place of entry or exit in the EU and the final destination are not the same. The statistical register considers the place of loading, although many goods are shipped to other countries in the internal market<sup>5</sup>. This unduly overrides the role of some major trading countries.

## Results

If we look at the 2018 data, the UK's main trading partners are mainly EU countries. Regarding agricultural and food trade the leading is Netherlands, Ireland, France, Germany, Spain, Italy and

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<sup>3</sup> In terms of the potential economic scenario of Brexit, the fundamental issue is the relationship to the internal market based on the four freedoms after the termination of British membership. If, after legal separation, the UK were (to some extent) part of the internal market, it would not be excluded from the system of European integration in the real economy. The latter is called soft Brexit. While the irreversible abandonment of the internal market is the hard Brexit.

<sup>4</sup> These duties could be high: for example, the average duty burden on animal products in the EU is around 20%. In the EU, the average duty rate was 5.3% in 2014, slightly higher than in some developed economies. In the United States, this indicator was 3.5% (IMF 2016). In the WTO system, the United Kingdom either sets a higher MFN duty on imports from 60 countries with a preferential agreement with the EU or must remove all barriers to all WTO members.

<sup>5</sup> For Belgium and the Netherlands, the statistical values may be inaccurate. The ports in Belgium and the Netherlands are major transit hubs. Through them, the United Kingdom's mainland, European and global trade flows. Some of these "Belgian" and "Dutch" exports originate from the continent or the rest of the world. Some of the imports from the UK are not for Belgian or Dutch but for further markets. Statistics Netherlands (2016),

Belgium. (Table 1.) At the same time, it should be noted that Ireland is the most heavily involved in British trade, 54% of UK imports comes from Ireland, and 58% of exports flow to the Irish market.

Table 1.: The UK's main agricultural and food trading partners related the amount and proportion of trade turnover, 2018

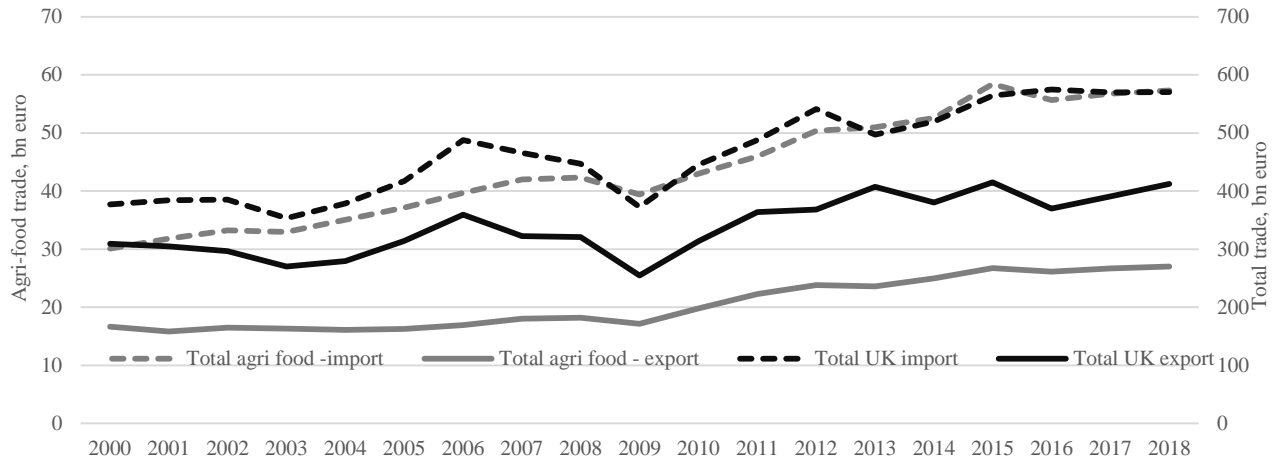
| Partner countries  | UK import |        | Partner countries                 | UK export |       |
|--|-----------|--------|-----------------------------------|-----------|-------|
|  | amount    | share  |                                   | amount    | share |
| Partner countries with the highest turnover amount – million euro, % |           |        |                                   |           |       |
| Netherlands  | 7 812,3   | 11,4%  | Ireland                           | 4 979,8   | 58,4% |
| Ireland  | 5 636,1   | 54,3%  | France                            | 2 628,3   | 5,8%  |
| France   | 5 346,8   | 13,3%  | United States                     | 2 553,9   | 11,5% |
| Germany  | 5 196,3   | 8,8%   | Netherlands                       | 2 038,5   | 5,8%  |
| Spain  | 3 808,8   | 10,6%  | Germany                           | 1 683,3   | 2,3%  |
| Italy  | 3 261,7   | 12,0%  | Spain                             | 1 158,3   | 5,6%  |
| Belgium  | 2 936,5   | 8,9%   | Belgium                           | 840,8     | 3,2%  |
| Poland   | 2 312,5   | 9,8%   | China                             | 712,9     | 6,8%  |
| United States  | 1 735,0   | 14,0%  | Italy                             | 686,6     | 2,2%  |
| Denmark  | 1 679,5   | 12,9%  | Hong Kong                         | 534,0     | 14,8% |
| Partner countries with the highest turnover share – million euro, %  |           |        |                                   |           |       |
| Montserrat   | 0,0       | 100,0% | Saint Helena                      | 3,1       | 99,9% |
| Niue   | 0,0       | 100,0% | Falkland Islands                  | 7,5       | 91,0% |
| Saint Barthelemy   | 0,2       | 99,4%  | Bhutan                            | 0,7       | 71,5% |
| St Lucia   | 6,4       | 91,1%  | Pitcairn                          | 0,2       | 71,1% |
| Macao  | 0,1       | 85,4%  | American Samoa                    | 0,1       | 69,6% |
| St Vincent and the Grenadines  | 0,7       | 83,0%  | Ireland                           | 4 979,8   | 58,4% |
| Jamaica  | 41,4      | 70,2%  | St Vincent and the Grenadines     | 4,8       | 54,4% |
| Djibouti   | 4,0       | 68,1%  | Heard Island and McDonald Islands | 0,0       | 51,8% |
| Micronesia   | 0,0       | 65,7%  | Antarctica                        | 0,2       | 48,7% |
| St Kitts and Nevis   | 0,6       | 56,4%  | Montserrat                        | 0,2       | 38,0% |

Source: own editing based on Eurostat 2019

At the same time, the UK is much more exposed to imports from EU Member States than to exports, both in terms of proportion and amount. As a result, the British market is more interested in gaining access to EU products and less in the UK to deliver to EU markets. It is also a peculiarity that the UK can even undo the entire EU agricultural and food trade with some countries. This is mainly due to British historical traditions and former colonial relationships such as Montserrat or Niue.

If we look at UK exports, we can see that the trade in agri-food products has gradually expanded across the entire trade. (Figure 1.) The expansion of trade flows has also had a positive impact on this product group. At the same time, the importance of the sector has increased over the past 18 years, with imports rising from 8% to 10%, while exports rose from 5.5% to 6.5%. At the same time, for the whole British trade, the impulse in agricultural and food products is significantly higher than exports. While, for example, in 2018, in the case of total foreign trade, imports are 35% higher than exports, while in agriculture and food products this figure is 112%.

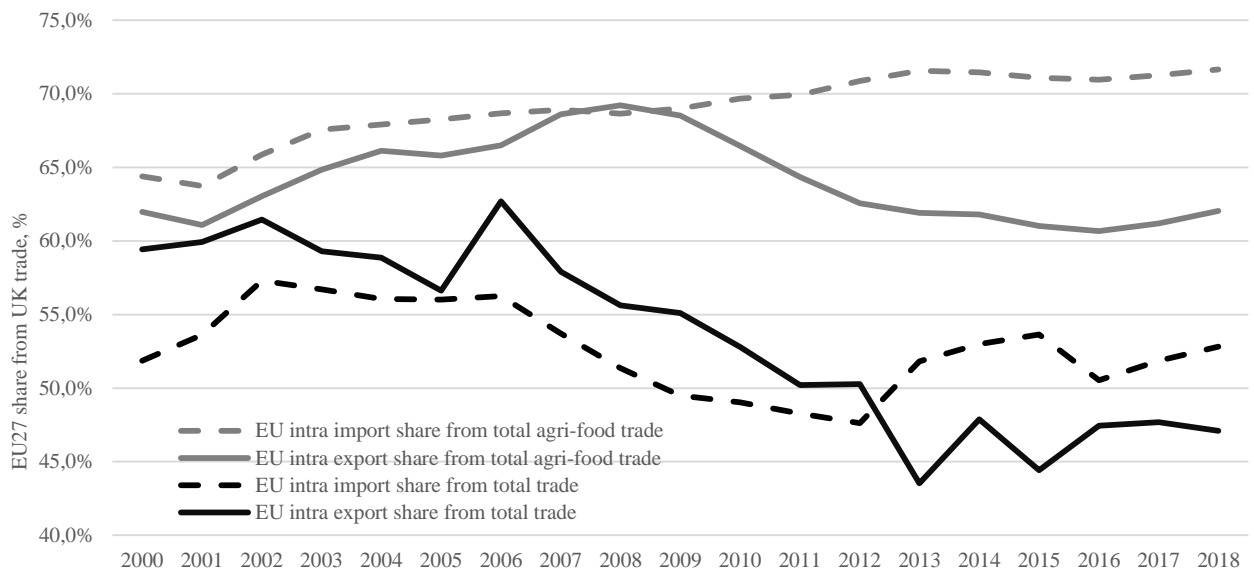
Figure 1.: The value of UK's total trade and agri-food trade (2000-2018, bn euro)



Source: own editing based on Eurostat 2019

Figure 2 illustrates the importance of the EU trade relationship with British trade. While the share of EU Member States decreased in total foreign trade, it increased to agricultural and food industry products. Therefore, in 2018, imports accounted for 71.6%, while exports accounted for 62% in case of agricultural and food industry products in relation EU countries. In case of total trade flow 47% of imports and 53% of imports coming from EU Member States.

Figure 2.: The importance of intra EU trade related UK (2000-2018, %)



Source: own editing based on Eurostat 2019

If the UK leaves the EU and does not sign a trade agreement, the MFN duty applies to bilateral trade between the United Kingdom and the EU27. The EU-27 average MFN customs duty on imports from the United Kingdom, according to preliminary estimates, is 18.3% and 3.2% for agricultural and industrial products, while EU exports are 14.2% and 2% respectively. An average load of 6% would apply. Agricultural products benefit from higher MFN protection. This reflects the importance of sensitive sectors such as sugar, cattle (meat and dairy products) and animal products in this area. After processed foods, the second most protected export sector is dairy products and meat products. Despite being of lower value, these two sectors rank second and third as they enjoy a very high level of protection: the MFN duty for dairy products is about 40% and NTMs are between 42% and 74%. in the case of meat products, 22% is duty-free and 43% has an impact on non-tariff measures.

For UK exports to the EU, the main exported products are valued at food and beverages. However, if we consider the impact of market protection, dairy products, beef and other meat products, the most protected products. For example, the effect of average protection would be more than 130% customs duty for dairy products if all the administrative (protective) measures were considered. EU27 is also less dependent on imports from the UK. These imports represent between 3% and 8% of all European imports in the sectors concerned.

Due to the expected transformation of the trading conditions, the role and the foreign trade significance of several product and product groups will change. Since the UK exports mainly to the EU, partly due to geographical opportunities, it is justifiable to look at what products may be important in a post-exit market. The most important export products are beverages, spirits and vinegar, meat and edible meat offal and dairy produce.<sup>6</sup> (Table 2) These three categories give one third of total UK exports. A significant part of British foreign trade is processed products or finished products. The export trends show, that bulk goods, such as cereals, represent the largest share in 2000, but in 2018 drinks jumped to the top. The amount of other processed products is also significant. 75% of British export products are semi-finished and finished products. Similar products appeared in imports, along with fresh goods (meat, milk, vegetables). As a result, they have a higher added value and consequently a greater margin. So, they may partially be able to compensate for the burden of hard Brexit and moreover transport costs.

Table 2.: The UK's most important agricultural and food export categories (2018, %)

| Categories   | Intra EU export share |
|--|-----------------------|
| Beverages, spirits and vinegar   | 13,08%                |
| Meat and edible meat offal   | 10,53%                |
| Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere Specified or included | 8,50%                 |
| Preparations of cereals, flour, starch or milk; pastrycooks' products  | 8,16%                 |
| Preparations of vegetables, fruit, nuts or other parts of plants   | 7,03%                 |
| Miscellaneous edible preparations  | 7,02%                 |
| Edible vegetables and certain roots and tubers   | 6,93%                 |
| Preparations of meat, of fish or of crustaceans, molluscs or other aquatic invertebrates                         | 6,06%                 |
| Edible fruit and nuts; peel of citrus fruits or melons   | 5,41%                 |

Source: own editing based on Eurostat 2019

## Conclusion

It can be concluded that unexpected and hard Brexit would have unexpected consequences. Avoiding it is a basic requirement for all parties. In the absence of post-exit conditions, a fundamental uncertainty factor at EU and British level should be considered for the economy, including agriculture and the food-producing industries, as well as trade. Because the need and necessity of covering domestic needs is crucial<sup>7</sup>, so the volume and composition of exports may even fall. Brexit - regardless of the outcome of the negotiations - is expected to have a minor impact on the market for British grain, vegetable oils and other agricultural commodities. However, Brexit is expected to have a significant impact on low-income semi-processed products in the EU. It is not expected that there

<sup>6</sup> At the same time the share of goods in non-EU markets is strong. 53% of total agricultural and food exports outside the EU belong to the group of drinks and tobacco products. In this trend, British, Scottish and Northern Irish spirits and other alcoholic beverages, as well as British tobacco products, play a decisive role.

<sup>7</sup> In the case of food, the United Kingdom can only satisfy 61% of its internal consumption. (House of Lords, 2017)

will be any substantial market reorganization for drinks, dairy products and other processed food products from the UK (eg chips).

Immediately after the British exit, non-tariff issues are unlikely to pose a major obstacle, as European and British legislation – because UK is a member – is essentially the same. However, in the medium and long term, issues relating to the mutual recognition of production standards, animal and plant health rules (previously organized within the Single Market) are of fundamental importance for future trade relations between the EU27 and the United Kingdom.

There is a clear need to underline: for the United Kingdom, the no deal option would have disastrous consequences. This option has serious implications for UK agriculture. Since the issue is not yet solved, the EU non-agreement exit is one of the biggest problems, and the acquisition of third-country certification should also be mentioned. This is an indirect effect. The UK may have at least six months to obtain a third-country supplier qualification. After leaving the European Union, British producers would go beyond the external borders of the European Union. Britain is fully compliant with EU legislation based on EU membership. However, in the absence of an agreement, going outside the EU would be subject to the same health rules as the UK. Should apply to suppliers in China or the United States.

Another point is that the lack of logistical capacities and physical checkpoints makes it difficult to export British products. If the United Kingdom were able to manage the rules for products subject to animal and plant health standards, the real possibility of shipping via the Dover-Calais route would be limited.

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