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Brexit: ultimately it's trade that matters

SEAN RICKARD[1]

1. Introduction

Officially the NFU of England and Wales has declined to take a position ahead of the conclusion of the UK government's renegotiation on future EU membership. It argues that until the details of an agreement are revealed it is impossible to measure the impact of Brexit on British farmers (NFU, 2015). That said, it would be surprising if the majority of British farmers did not fear that their businesses would suffer if the UK voted to leave the EU. Unconstrained by the Common Agricultural Policy (CAP) a British government would be free to reduce the level of financial support for the sector and terminate agricultural exceptionalism thereby placing farming in the same position as industries in general. Before considering the implications in more detail it is worth pointing out that reports suggesting that Brexit would be devastating for UK agriculture (see for example Agra Europe, 2015) fail to fully allow for the fact that the impact of lower financial support on production would be mitigated by a reduction in the industry's cost base and restructuring towards more productive, larger scale farms.

As the government has not made any pronouncements regarding agricultural policy if freed from the CAP we must rely on previous governments' submissions for guidance. In 2005 the Labour government published its 'vision for the CAP' (Treasury, 2005) and in advance of the 2013 CAP reform the Coalition set out its objectives (Defra, 2011). Both publications argued for the phasing out of decoupled payments – broadly the CAP's Pillar I, Basic Payments Scheme (BPS) – while continuing to finance agri-environment schemes and rural development ie, payments falling under Pillar II. As Pillar I payments amount to about three quarters of CAP expenditure and de facto, serve largely as income augmenting social payments, this appears to threaten a substantial reduction in farm incomes. In a detailed study published in the run-up to the 2013 CAP reform, the Commission argued that phasing out direct payments would lead not only to much larger and more capital intensive farms but also production systems would become more intensive in the most productive regions and land would be abandoned in less advantageous areas (Commission, 2011).

On the basis of this and other studies it might seem reasonable to expect that structural change along the lines projected by the Commission would be manifest in the UK if the level of farm support was rapidly reduced. However, there are two reasons to suspect that in the event of Brexit, the structure of UK agriculture would not vary markedly from what it would otherwise have been in the following years. Firstly, structural change involving a steady decline in the number of farm holdings has been a feature of UK agriculture since 1945. There are currently 212,000 farm holdings in the UK but some three quarters of the agricultural area is farmed by just 42,000 holdings (20 per cent) with an average size of 304 hectares. The numbers of these larger scale farms have remained relatively stable over recent years whereas the population of smaller scale holdings has declined steadily. This pattern is likely to continue whether or not the UK remains within the EU, particularly as farms with an area of less than 5 hectares in England and Wales – 3 hectares in Scotland and Northern Ireland – are not eligible for support under the BPS.

Secondly, despite the declared intention to reduce support, neither Party's submission on the future of the CAP set a time table for the removal of decoupled payments. There are good reasons to doubt that the overall reduction in public expenditure on agriculture would be as large as indicated. The pace and extent of reform, following Brexit, would be subject to negotiation not only with the devolved administrations in Scotland, Wales and Northern Ireland but also with the NFU and other lobbies. The devolved administrations are supportive of the BPS as a significant proportion of their farms would be vulnerable by virtue of their smaller scale and more difficult geography. Thus, there would be pressure to retain current levels of spending and, I suspect, pressure to limit any redistribution towards the more prescriptive Pillar II type schemes. And should English farmers be threatened with a steeper cut in decoupled payments than their counterparts in the regions the NFU would mobilise its considerable political influence. More generally the government would face the political charge that by phasing out decoupled payments it was subjecting British farmers to an 'uneven playing field' and there might be claims for compensation. That said, even with transitional arrangements spread over a period of years the likelihood is that UK decoupled payments would decline relative to EU payments in the years following exit.

Moving beyond financial support; previous UK government submissions have argued for the removal of remaining trade barriers and greater liberation for farmers in making decisions regarding their businesses. This suggests that outside the EU competitiveness would replace social welfare as the primary policy objective. But again, it is far from clear to what extent a future government would remove existing regulations. Leaving

Original submitted November 2015; accepted January 2016.

[1] sean@seanrickardltd.co.uk, Sean Rickard Ltd. www.seanrickard.co.uk

trade matters aside for the moment, consumer, environmental and public health organisations have considerable political influence and would argue forcibly against any moderation of existing EU Directives regarding pollution eg, nitrate and pesticide leaching, water quality, birds, habitats and animal welfare.

A more likely change would be a more positive attitude towards the frontiers of agricultural science and technology. No longer subject to the CAP's voting rules, a British government is likely to more aggressively support the adoption agro-biotechnology as a means to improving competitiveness. Further, both farmers and their suppliers would benefit from the UK's exit from the EU's long drawn out, opaque system for approving new pesticide products. There is however, a question as to how quickly British farmers would take-up the more controversial technology of genetic modification. Although a recent survey showed that only 14 per cent of UK consumers are strongly opposed to GM foods, 82 per cent remain undecided or hold only mildly positive or negative opinions (IGD, 2014).

Given a focus on international competitiveness of key importance would be the UK's post exit trade relationship with the EU. There are in principle four trade relationships that the UK could seek with the EU (House of Commons (a), 2013): a highly integrated option of a European Economic Area (EEA) agreement; a less conditional European Free Trade Area (EFTA) agreement; a UK specific preferential Regional Trade Agreement (RTA); or resort to a WTO most-favoured-nation (MFN) agreement. Unfettered access to the single market would be a priority for the food industry but this is an unlikely outcome. An EEA agreement would appear to offer the greatest likelihood of equivalence to existing arrangements. However, the House of Commons Foreign Affairs Committee inquiry into the UK's future relationship with the EU concluded… *we agree with the Government that the current arrangements for relations with the EU which are maintained by Norway, as a member of the European Economic Area, or Switzerland, would not be appropriate for the UK if it were to leave the EU* (House of Commons (b), 2013, pp9). A position reiterated by the Prime Minister in his recent speech to the Northern Future Forum in Iceland.

Presumably, the government's preferred option would be to negotiate a preferential RTA. The Out campaigners assert that a satisfactory RTA could be negotiated but they provide no articulation on the details of such an agreement. They rely on the argument that as the UK has a persistent trade deficit with the EU in food and agricultural products – £16.4bn in 2014 (Defra 2014) – it would be in the EU's interest to reach a negotiated bilateral agreement on such products. However, a key issue would be the willingness of the EU to enter into a preferential RTA if it did not include the four 'freedoms' involving the movement of goods, capital, services and people that are conditional in the EU's treaties with the EEA and EFTA. Even if the UK negotiates a way round the free movement of people it is unlikely that UK agriculture, and businesses in general, could retain all the trade freedoms eg, mutual recognition, currently enjoyed within the single market – the consequence of which would be to devalue membership of the EU for remaining members.

If a satisfactory preferential RTA proved unnegotiable the UK would have to revert to existing WTO agreements. In this situation as the prospect of a new multilateral trade agreement is now vanishingly small, UK farm and food exports to the EU would face both tariff and non-tariff barriers. To take but one of many examples of the former: exports of cheddar cheese with a minimum fat content of 50 per cent would face a tariff of €167.1 per 100kg. Non-tariff barriers would primarily be concerned with compliance eg, UK exports would be subject to the CAP's regulations concerning maximum pesticide residues. Indeed, the idea that outside the EU the government would have complete freedom of action regarding agricultural policy is a fiction; even its WTO commitments impose constraints. Given that the EU will remain an important trading partner, the UK would find it in its self-interest to align its regulations and standards closely to those in force in the EU. And in many areas of food and agricultural policy, EU standards are based on existing WTO standards eg, Codex Alimentarius. Paradoxically, the adoption of GM technology by UK farmers would not pose a problem as despite the EU's almost complete moratorium on growing GM crops the same products can be imported from non-EU countries. This still leaves the issue of the EU's existing RTAs with third countries. Presumably, the UK would seek to negotiate new RTAs with these countries in order to continue with the EU's tariff preferences. But there might be opposition; for example, Brazil might protest if the UK offered tariff concessions on raw sugar to Least Developed Countries (LDCs) as if it were still applying the EU's Economic Partnership Agreements.

2. End Piece

There is little prospect of the CAP's multifunctional approach to agricultural support changing significantly in the foreseeable future. This suggests that in the event of Brexit, UK agricultural policy reform is likely to move at a faster pace and also in a direction that gives primacy to productivity and competitiveness. While this consequence is to be welcomed arguably of more importance would be the extent of the food and agricultural industries' access to the single market. Despite the claims of Eurosceptics it is impossible at this time to anticipate how successful the UK might be in this endeavour or how long negotiations would last. The inevitable uncertainty could result in longer term adverse consequences; such as, some multinational food companies relocating to other parts of the EU. Finally, those hoping for a rapid reduction in wasteful public expenditure on agriculture are likely to be disappointed as powerful lobbies would bring their influence to bear to minimise the cuts and to prolong the transitional period.

About the author

Sean Rickard PhD, MBA, MSc, BSc, FHEA, RiVF, was for 10 years Chief Economist for the National Farmers' Union before joining the Cranfield School of Management in 1995 where inter alia he was Director of the MBA Programme. After leaving the NFU he was for 17 years appointed as a government academic economic advisor on food and farming matters. Since retiring from Cranfield in 2012 he has established a consultancy specialising in these areas and is a visiting research fellow at the Royal Institution. His book, The Economics of Organisations and Strategy is published by McGraw-Hill.

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