Teagasc Opening Statement, Seanad Select Committee on the impact of withdrawl of the United Kingdom from the European Union, Seanad Éireann, May 18 2017.

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Chairman, Senators

Teagasc thanks the Seanad Special Select Committee on the withdrawal of the United Kingdom from the European Union for the invitation to this meeting. My contribution will be with respects to the agriculture and food sector.

Chairman, in your invitation you asked that my presentation focus on what challenges for Irish agriculture we have identified as arising from the UK decision to leave the UK, the solution or solutions that we believe might best address the challenges identified, what relevant precedents exist if any and how any solutions might be implemented.

In my opening statement I will focus on the challenges for the Irish agri-food sector that Teagasc has identified as arising from Brexit and actions that Teagasc has undertaken in relation to Brexit and the role that we see Teagasc playing as the Irish agricultural and food industries confront the competitiveness challenge posed by Brexit.

Solutions to address these challenges are difficult to specify in detail at this point in time given the continuing lack of clarity as to the nature of the Brexit that will unfold and the nature of the trade relationship between the UK and the EU, between Ireland and the UK and within the island of Ireland (North-South) following Brexit. However it goes without saying that Teagasc is of the opinion that the best outcome from the perspective of Irish agriculture is an outcome that involves as little change as possible to existing nature of the trading and other relationships that exist between Ireland, the EU and the UK.

Brexit could represent one of the largest competitiveness shocks that the Irish agri-food industry has faced. The key role of Teagasc as the Ireland Agricultural and food development authority is to provide the research, knowledge transfer and education to Irish farmers and the Irish food industry that will enable it to survive and thrive in what, because of Brexit, will be a more challenging economic environment.

Challenges identified

The key challenges posed by Brexit that we have identified relate to

a) **The potential loss of preferential market access to the UK for Irish agri-food (and other) exports**. As members of the EU Customs Union and Single Market Irish, UK and EU agriculture and food markets continue to enjoy significant levels of tariff protection vis à vis imports from non-EU sources. This reflects a principle of the Common Agricultural Policy (CAP) known as *Community Preference*. Despite cuts in the levels of tariff protection afforded to the EU agri-food sector that were agreed in the Uruguay Round of the GATT in 1994, EU agricultural and food tariffs remain high. In the absence of a Free Trade Agreement (FTA) between the EU27 and the UK, trade relations between the UK and the EU will revert to WTO rules. This would mean that UK exports to the EU would face the EU common external tariff, which for many agricultural goods is very high. After exiting the EU the UK will inherit the EU tariff schedule bindings. The UK, in the absence of a FTA with the EU, could choose to apply lower rates than its WTO binding, but it must offer these applied rates to all other WTO members ("most favoured nations"). This would mean that even in the unlikely event that the UK unilaterally liberalised all of its applied tariffs and Ireland had tariff free access to the UK market this access would no longer be preferential, since all other WTO members would have similar terms.

b) **The potential negative impact of Brexit on trade and all-island (North South) supply chains in agricultural and food products**. If following Brexit tariff and non-tariff barriers to trade emerge on the Island of Ireland trade and supply chains between Ireland and Northern Ireland (North South) will be disrupted. Within overall Ireland-UK agri-food trade, trade along the North-South axis (approximately 14% of Ireland-UK agri-food trade) is dominated by East-West trade between Ireland and Great Britain. The nature of the products exported from Ireland to Northern Ireland (and to Great Britain) also differs importantly from the products imported from Northern Ireland. Imports of agri-food products from Northern Ireland are dominated by imports of raw unprocessed milk, with almost 80% of the value of imports made accounted for by milk imports. Ireland's exports to Northern Ireland are more diverse. The only flow at the tariff line level that accounts for more than 10% of the overall exports flow from Ireland to Northern Ireland are exports of butter. Potential barriers to trade in raw milk will pose major challenges both for Northern Irish farmers supplying milk to Southern processors and major challenges to Southern based milk processors with a significant portion of their intake supplied by Northern Irish farmers.

c) **The impact of non-tariff barriers to trade with other parts of the EU Single Market arising from Brexit.** Brexit will impose additional non-tariff barriers to trade between Ireland and other parts of the EU Single Market due to the routing of a large proportion of Irish agri-food trade with continental EU markets the UK "land bridge". Customs clearance procedures will apply if as seems likely the UK leaves the EU Customs Union. Additional costs (non-tariff barriers) will be imposed on Irish merchandise exports on entry to and exit from the UK. This will impose what in our opinion will be a unique burden on Irish exports to other parts of the European Single Market. The competitiveness of Irish agri-food exports to continental EU markets will be reduced by even the softest Brexit. The additional costs associated with customs clearance and the likely increase in the time it takes to get products to market will be particularly onerous for businesses selling perishable goods.

d) **Impact of Brexit on the EU budget and the CAP budget**. The UK is currently the second largest net contributor to the EU budget. Brexit will reduce the quantum of financial resources within the EU budget unless other Member States increase the size of their contributions. On the assumption that other MS do not fill the budget "hole" created by Brexit, spending on EU policies and programmes (including the CAP) is likely to fall. Spending on the CAP currently accounts for almost 40 percent of EU spending it is hard to envisage spending on the CAP being unaffected by Brexit. Lower CAP spending, particularly on Pillar 1 measures such as the Basic Payment would have significant negative impacts on agricultural incomes in the Ireland and across the EU.

e) Other important challenges that will arise because of Brexit relate to future divergence in regulatory standards between the EU and the UK. The requirement to satisfy UK standards that might in the future diverge from EU standard will impose additional costs on Irish agri-food exporters that supply this market in the future.

More information on the challenges

Trade policy and tariff and non-tariff barriers to trade

The magnitude of the competitiveness challenge posed by the introduction of tariff and non-tariff barriers to agri-food trade between Ireland and the UK and between Ireland and the other Members of the EU will be a function of the current level of dependence on the British and continental EU markets and height of the tariff and non-tariff barriers that will emerge post-Brexit.

At this point it is not clear what whether or not there will be a FTA between the UK and the EU that will maintain the mutual preferential access to another's markets that is currently enjoyed. If the UK leaves the customs union and if Brexit occurs without an agreement that maintains the current completely free trade arrangements additional tariff and non-tariff barriers to trade will arise both on Irish trade with the UK. Additional non-tariff barriers will also arise for Irish trade with the rest of the Single Market due to the role of the UK as a physical route to continental EU markets.

The maximum tariffs that could apply to Irish agri-food exports to the UK following Brexit in the event that no FTA between the EU and the UK is agreed are known. These are the EU tariff bindings as notified to the World Trade Organisation (WTO) that the UK will "inherit" once it leaves the EU. There are almost 2,500 tariff lines relating to agricultural and food products and these EU (and future UK) tariff bindings are a mixture of specific tariffs (e.g. euro per 100 kg), ad valorem tariffs (% of the landed goods price) and compound tariffs that combine specific and ad valorem components.

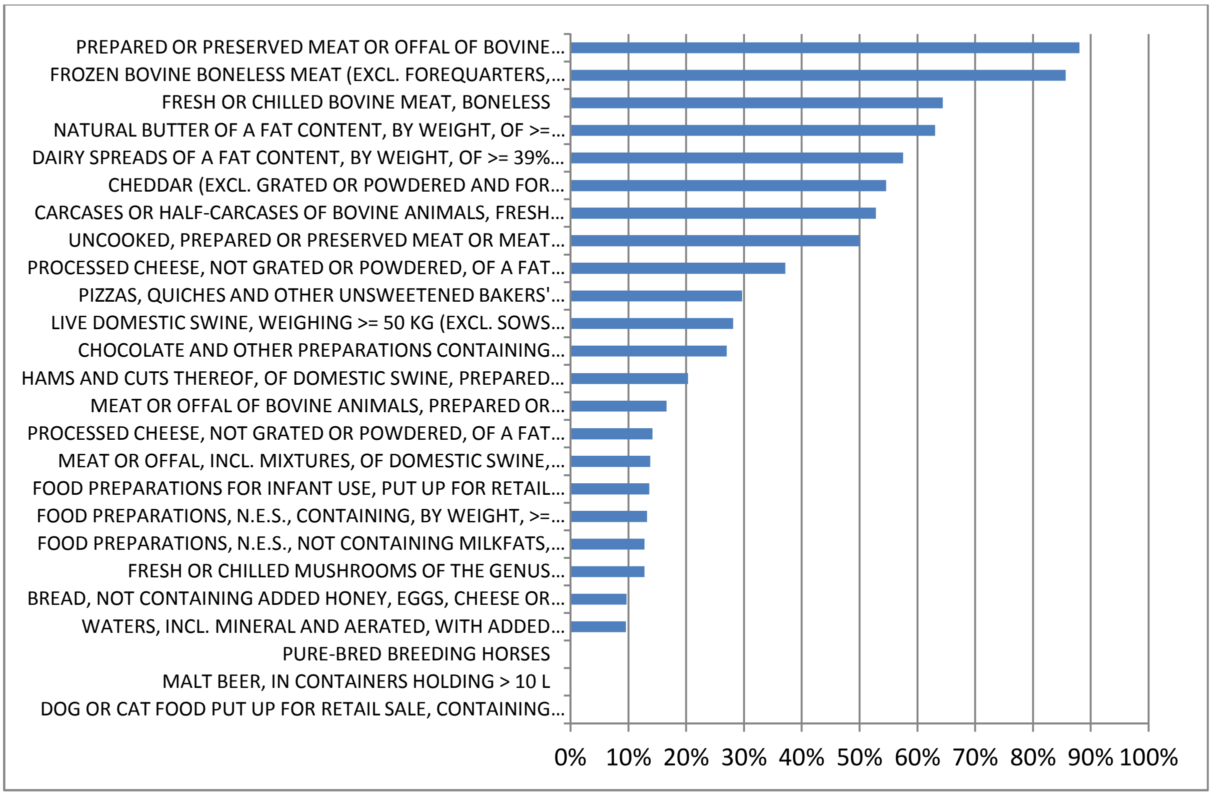
Using data on imports of agri-food products by the UK from Ireland it is possible to calculate what are known as *ad valorem equivalents* for each of the tariff lines where trade exists between Ireland and the UK. Analysis at the tariff line level highlights the very high levels of bound tariffs that could apply to important elements of Ireland's agri-food exports to the UK.

Rather than attempt to graph all of the tariff lines and their ad valorem equivalent, agri-food trade flows at the tariff line level between Ireland and the UK were ranked by value and ad valorem equivalents of the MFN bound tariff levels were calculated for the top 25 tariff lines when ranked by value. These top 25 tariff lines in the UK imports of agri-food products from Ireland accounted for over 60% of the value of UK imports of agri-food products from Ireland.

In Figure 1 the tariff lines are ranked in order of the magnitude of the calculated ad valorem equivalent of the MFN bound tariffs. The most valuable trade flow from Ireland to the UK when measured at the tariff line level in 2015 was fresh boneless beef (bovine meat). In 2015 the imports by the UK from Ireland for this tariff line were worth almost €540 million, the ad valorem equivalent of the WTO MFN bound tariff calculated using 2015 trade data is 64%. UK imports of cheddar cheese from Ireland in 2015 were valued at over €300 million and would, at bound MFN rates, face an ad valorem equivalent tariff of 55%. These tariff rates are prohibitive and at plausible measures of the responsiveness of trade to prices (what economists call price elasticities) destroy this trade flow.

Research by colleagues at the ESRI has using trade elasticities for agri-food as an aggregate concluded that much of the trade between Ireland and the UK in agri-food products would disappear. The magnitude of the ad valorem equivalent of the bound tariff levels calculated at the tariff line level would support such conclusions.

Figure 1. Top 25 agri-food tariff lines for UK imports from Ireland: Ad valorem equivalent of EU MFS tariff bindings



Source: Based on Eurostat COMEXT data on UK agri-food imports and EU WTO tariff bindings.

Goods not exported to the UK in the event of a very hard Brexit would be diverted to other markets in the remaining EU27 and outside of the EU. Almost certainly such diverted trade flows would return lower value to Irish agri-food exporters with the diversion of large volumes of Irish beef, butter and other agricultural commodities to other EU markets likely to also lead to lower prices in these markets that might reasonably have been expected to prevail if Brexit was not happening. Teagasc analysis conducted in advance of the UK referendum of June 2016 indicated that the loss of agri-food export value could approach €1 billion euro (Donnellan and Hanrahan, 2016). This early estimate of the loss of agri-food export earnings may represent an underestimate of the impact of Brexit and research is on-going in this area.

If a firm is largely exporting goods to non-EU markets Brexit may not directly affect their current terms of trade but will limit the extent to which they can exploit market opportunities in the UK following its exit from the EU. Firms (or industries) that export large proportions of output to the UK markets will be directly affected by the introduction of tariff and non-tariff barriers to trade. Firms (or industries) where exports that are predominantly shipped to continental EU markets via the UK "land bridge" are likely to incur additional costs in getting products to markets, even if the tariff barriers to trade with other parts of the Single Market are unaffected by Brexit.

Implications of Brexit for the EU Budget, the CAP budget and Irish agricultural incomes

Irish agricultural sector income and family farm incomes continue to rely heavily on decoupled direct income supports from the EU Common Agricultural Policy. The CSO preliminary estimate of agricultural sector output, input and income for 2016 shows that direct payments accounted for almost 60% of aggregate agricultural sector income. In 2015 the Teagasc National Farm Survey found that the direct payments accounted for 65% of average family farm income. The dependence of family farm income on direct payments was highest on Cattle Rearing, Cattle Other and Sheep farms where direct payments accounted for either close to or over 100% of family farm income. Brexit will negatively affect the size of the EU budget and the agricultural component of that budget. It seems likely that a smaller EU budget and a smaller CAP budget will reduce the level of direct income supports received by Irish farmers and also reduce the quantum of budgetary resources that Ireland receives from the EU.

The increase in the tariff and non-tariff barriers faced by firms exporting to the UK will mean that efforts to continue to reduce the reliance on the UK market will have to continue. In the event that the UK leaves the EU without a FTA being agreed and applies its' current WTO tariff bindings to agri-food trade large parts of existing agri-food trade flows between Irish and UK markets might cease. EU bound MFN tariffs on agri-food trade are prohibitive by design. The application of such high tariffs by the UK would likely lead to increases in UK food prices given its status as a large net importer of agri-food products. The UK might choose to apply lower tariffs than its WTO bindings. In this case Ireland would face at best the zero tariff levels it currently faces when exporting to the UK but would find itself competing in a changed UK market with other WTO exporters who heretofore were excluded from the UK market by high EU tariff barriers. Our preferential access to the UK market is what makes this market so valuable. Brexit will at worst end this preferential access and even if a FTA between the UK and the EU can be agreed it will reduce the value of that preferential access.

What solutions might address the challenges identified?

What solutions can be envisaged that will mitigate the impact of such developments? From the perspective of the overall sector and Irish society and economy the Government's objective of trying to minimize the extent to which Brexit changes the status quo ante in terms of the trade relationship and other relationships between the UK and Ireland and the EU makes complete sense. However, in the event that the outcome leads to tariff and non-tariff barriers to trade between Ireland and the UK and Ireland and the rest of the Single Market and assuming the withdrawal of the UK from the EU negatively affects the size of the EU budget

The challenges identified represent a competitiveness challenge to the Irish agri-food sector. To address this competiveness challenge will involve actions that augment the productivity and efficiency of Irish agricultural production and Irish food manufacturing as well as actions that facilitate access to new markets for Irish exports and assist in the development and growth of existing markets.

Increased exports to markets other than the UK will be hard won and such successes in the future will rely on Irish agri-food exports being competitive in terms of prices and competitive in terms of the attributes of the products produced and offered to consumers. Innovation in the farm and food processing industries will be critical in ensuring that Irish agri-food exports are competitive in terms of costs of production and price. Innovation, particularly in the Irish food processing industry, will be critical in developing new products and adding to the attributes of existing products that will enable them to capture new markets and increase market share of existing markets in the EU27 and the rest of the world. The State and EU will have a role to play in supporting research, knowledge transfer and education that supports the development of an innovative and productive Irish agri-food sector. Teagasc as the Irish Agricultural and Food Development authority is clear on the importance and role that its agriculture and food research, knowledge transfer and education programmes will have in supporting the Irish agri-food industry to face and overcome the competitiveness challenges posed by Brexit.

The outcome of the Brexit process is currently a “known unknown”. However, we can be confident that even the “softest” Brexit will lead to some deterioration in the nature of the economic relationship between Ireland and the UK and between the EU and the UK. There will be additional costs to doing business between the EU and the UK after Brexit that will arise as a result of tariff and non-tariff barriers and the divergence over time in our common standards and regulatory frameworks. Thus the magnitude of the additional competitiveness challenge posed by Brexit is still to be revealed. The magnitude of the challenge will in part will be determined by the nature of the Brexit outcome. Depending on the nature of the Brexit outcome there will be a need for a reassessment of the resourcing of support to agri-food research, agricultural extension and education that will equip the agriculture and food industry in Ireland to survive the shock that Brexit will pose and equip the industry to thrive following the eventual exit of the UK from the EU.

The solutions offered to the competitiveness challenge, become more competitive and innovative, increase productivity and diversify markets, may appear like old wine in new bottles- and in a sense this criticism is legitimate. However, the Brexit referendum result and the UK government’s seeming desire for what amounts to a hard Brexit, will transform the nature of the competitiveness challenge faced by Irish agriculture and food sectors. Given existing dependence on the UK, the impact of Brexit on existing access to the rest of the Single Market and on North-South trade within the island of Ireland as well as the potential impact of Brexit on income support to Irish farmers, Brexit demands increased emphasis on and resources for efforts by Teagasc and others that augment the capacity of Irish famers and food industries to survive and thrive post-Brexit.