March 2017

Policy briefing

Post-Brexit trade policy and development

Current developments; new directions?

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Key findings

- Many developing countries rely on trade with the UK to create jobs, boost economic growth and reduce poverty: 9% and 8% of exports from Bangladesh and Kenya, respectively, go to the UK.
- The emerging new UK trade policy seems to be primarily based on bilateral agreements. Developing countries will be harmed, especially if their current trade arrangements are not secured or improved: least developed countries (LDCs) could lose approximately £323 million annually if preferential access to the UK is discontinued.
- To date, there has been little or no consideration by the UK government of Brexit's impact on developing countries or an assessment of the opportunities that Brexit may present in terms of trade and development cooperation. For example every pound of bilateral aid leads to a 22 pence increase in UK exports. In 2014, £5.1 billion in UK bilateral aid increased UK exports by almost £1.1 billion. This amount of exports creates 12,000 UK jobs.

Recommendations

- The UK's trade and international development policies should be aligned.
- The UK should apply the principle of 'do no harm' and avoid damaging developing countries as it leaves the EU.
  - Existing unilateral preference regimes should at least be rolled over and the UK should seek to go further.
  - The roll-over of existing Free Trade Agreements (FTAs), especially Economic Partnership Agreements (EPAs), with other developing countries needs to be prioritised.
- The UK's new trade policy should be simple, predictable, transparent and realistic.
  - The UK should simplify tariff structures by eliminating *non-ad valorem* duties and nuisance tariffs, and raising the thresholds of rates and VAT.
  - The UK should assess the effects of new FTAs on the poorest countries. Moreover, it should seek to negotiate provisions that benefit those disadvantaged countries, including among other things, cumulation in rules of origin.
  - In its negotiation with the EU, the UK should aim to include provisions on mutual recognition to avoid disrupting value chains involving poor countries.
- The UK should pursue 'win-win' options, such as more liberal rules of origin, preferential access in services and Aid for Trade.

Introduction

The UK will regain control over its trade policy when it leaves the EU. As it negotiates new FTAs around the world, all of the UK's current and future trading partners should be assured that they will not be worse off because of Brexit, and the UK should be clear that it is open to every country in the world.

The UK has committed to supporting the economic development of LDCs and trade is noted as a core priority in the UK Department for International Development (DFID)'s recently published Economic Development Strategy (DFID, 2017). As such, the UK's trade and development policies will need to work together and reinforce each other. Indeed, there will be many policies that are aimed at supporting developing countries, but will also benefit British businesses. This 'win-win' approach will ensure that the UK can successfully achieve both its trade and international development objectives.

Key findings

Emerging UK trade policy

The UK is currently in the process of designing a new trade policy that operates in at least four areas (see Box 1). This agenda has been designed with the aim of securing increased market access for British products and increased competition in the British market itself.

This approach seems to be based on a typical bilateral market access approach: the UK is willing to open its market in exchange for market access for its products. Beyond a commitment to the multilateral agenda that the UK already supports, this approach may be suitable for the biggest and most important trading partners.

Developing countries largely absent so far

To date, the UK has paid no attention to its trade relationships with the poorest developing countries, which have been absent from the discussions, speeches and debates. This has happened despite the risk that they could be significantly harmed by the UK's departure from the EU, with a number of important win-win opportunities missed in the process (te Velde, 2016).

Many developing countries do not have the technical and economic capacity to negotiate reciprocal FTAs with the UK. Along with this, the flexibility typically granted to developing countries in FTAs under Article 24 of the General Agreement on Trade and Tariffs (i.e. the 100% UK liberalisation and 80% partner country liberalisation rule) may not be feasible for these countries, particularly when import duties constitute a large source of fiscal income.

Without a solution to this market access issue, developing countries will face additional and costly duties. For example, LDCs will face a £323 million

Box 1. The four channels of UK trade policy: current directions

a) **WTO:** The UK is likely to roll over EU schedules in terms of tariffs. There will be some discussions on quotas in agriculture and Table 1 outlines what the UK's most-favourable nation (MFN) tariff could look like. For 23.9% of the tariff lines, the duty is zero; for an additional 7.1%, the duty is lower than 2%. However, there are also a significant number of tariff lines set above 15%.

Table 1. Descriptive statistics of the current EU bound tariff schedule

Simple average (%)	6.5
Standard deviation	12.1
Agricultural products (%)	14.6
Non-agricultural products (%)	4.4
Duty free tariff lines (%)	23.9
Nuisance applied rates (%)[1]	7.1
Domestic peaks (%)[2]	5.6
International peaks (%)[3]	8.8

Source: ODI elaboration based on WTO's EU Trade Policy Review 2015.

1 *Tariffs greater than zero, but less than 2%*

2 *Tariffs greater than three times the average duty*

3 *Tariffs greater than 15%*

b) **FTA with the EU:** Being the largest destination of UK exports and source of UK imports, not having free access to the EU will constitute a major shock for value chains linking both sides.

c) **Roll over of EU FTAs:** When examining the 27 largest export partners outside the EU, there are eight countries with an existing EU FTA (Chile, Egypt, Israel, Korea, Mexico, Norway, South Africa and Turkey) that could levy €1.2 billion more on UK goods if the UK were not party of a new FTA with them. Some transitional arrangement and deals would therefore need to be discussed. The UK is expected to roll over existing FTAs; however, some countries might seek change.

d) **Attempt to negotiate new FTAs with countries such as US, Australia and China:** While the UK cannot conclude deals before leaving the EU, it is nonetheless able examine the economic opportunities. For example, the UK may save $7.3 billion in duties paid and increase its trade by signing FTAs with Australia, Azerbaijan, Brazil, Canada, China, India, Japan, Malaysia, Nigeria, Qatar, Russia, Saudi Arabia, Taiwan, Thailand, the United Arab Emirates and the US.

annual bill in terms of tariff duties in the UK. Moreover, many of their competitors may have better market access to the UK as a result of the FTAs. Brazil, India and China, for example, tend to produce a variety of products (e.g. tropical fruits, sugar and/or light manufacturing) that compete with many poor developing countries' exports to the UK (Mendez-Parra, 2016).

Recommendations

1. The UK should apply the principle of 'do no harm' and commit to ensuring that the UK's exit from the EU leaves no developing country worse off.

Although UK trade policy will be primarily designed to seize opportunities and address challenges faced by the UK, there is a moral duty to avoid harming people living in developing countries. In this sense, the UK may have a responsibility to secure the continuation of preference regimes that favour developing countries.

The UK should therefore, at a minimum, avoid removing the existing benefits and current market access received by the world's poorest.

2. The UK's new trade policy should be guided by a number of principles and tests, including predictability, simplicity, transparency and realism.

These tests include:

- **Predictability:** The UK and other exporters need certainty regarding market access and other provisions.
- **Transparency:** The benefits of the trade policy must be available to everyone, avoiding discriminatory practices.
- **Simplicity:** Complexity in the design, application and compliance of provisions may constitute a major barrier to trade.
- **Realism:** Trade policy will also be subject to the policy objectives of other countries, particularly when based on bilateral agreements. Crucially, the UK's limited influence should be recognised, as there will be countries that do not feel any urgency to negotiate with the UK.

3. The UK's trade and development objectives should be aligned.

There are a number of areas where the UK can deliver an ambitious new trade policy and also achieve its stated international development objectives in relation to trade and economic growth.

Preferences

- The UK must continue providing preferences to LDCs. This will mean rolling over those existing in the area of Everything But Arms (EBA). This will provide certainty and avoid harming firms and people working in developing countries.
- However, this may not be enough. Many producers in developing countries, such as Pakistan, which today exports to the UK under the Generalized System of Preferences + (GSP+) and with whom the UK is not aiming to negotiate an FTA, need to have their market access secured. Consequently, the UK should aim to cover both LDCs and other developing countries – with whom negotiating FTAs may not be an option – in a unique, simple and full GSP regime.

Box 2. The importance of the UK market for developing countries

Although the UK has lost a share in the exports of developing countries over recent years, it nonetheless continues to be an important export destination for some. For Belize and the Seychelles, for example, the UK accounts for more than 25% of total export value (Mendez-Parra et al., 2016).

Bangladesh: Out of the total overall exports, 9% are to the UK. They are heavily concentrated on garments which, currently duty-free under the EBA preferential regime, may face tariffs of 6–12%.

Kenya: The UK accounts for 8% of total exports, with tea being the one of the highest value (which is zero-rated under the EU's MFN). However, about half of the total export value is accounted for by cut flowers and fresh fruit and vegetables. As it is currently eligible for standard GSP preferences (with the exception of flowers, for which it has been graduated out of the GSP on market share grounds) and an interim EPA agreement, Kenya may face tariffs ranging from 2% to 16% on these goods.

Pakistan: The UK accounts for 7% of total exports. The main products are various textile items and garments, along with rice, which is not covered by the GSP (aside from a separate EU-Pakistan agreement for long-grained brown rice). Pakistan is currently eligible for GSP+ preferences and could face tariffs of up to 12% on these exports.

Malawi: The UK accounts for 6% of total exports. Although over 40% of the value of UK imports is accounted for by tea (zero-rated under MFN), sugar and tobacco account for almost all of the remainder. Currently duty-free under the EBA regime, these products could face tariffs of up to 18.4% (tobacco) and over 50% ad valorem equivalent (sugar) after Brexit.

- The UK should go further and deepen this regime. This means making its rules of origin compatible with those in other FTAs that influence negotiation. It should also allow the cumulation of origin from other developing countries. In addition, it should maximise *de minimis* thresholds for products originating in LDCs.

FTAs

- The UK should aim to give the roll over of existing FTAs with developing countries higher priority in the negotiation. This is particularly important for those countries with whom trade is already covered by the Economic Partnership Agreements (EPAs) or other FTAs (e.g. Vietnam), to avoid serious market access challenges for these countries. It is important to recognise that many countries negotiated these agreements with the EU because the UK was its main trading partner (Stevens and Keenan, 2016).
- The UK should recognise and accept that these agreements with poorer countries often need to be negotiated on a non-reciprocal basis, with fewer commitments for developing ones. For these non-LDCs, the UK should aim to bear the largest part of the effort by applying the 100/80% rule.
- The UK should recognise that a) preferences will remain critical for countries without FTAs or EPAs and b) poor countries may be at risk of being left behind.

Box 3. Following citrus fruits from southern Africa to the UK

Some 100,000 people (Mokhema, 2015) are employed in citrus production in southern Africa and the UK absorbs 10% of their exports, with 78% of these exported to the UK through the Netherlands or Spain, where exporters and traders benefit from major logistic facilities for the produce (FreshFruitPortal.com, 2016). Moreover, as standards applied in the UK and the EU are the same, traders only need to certify the compliance of their products once. This also benefits consumers, as the lower costs are translated into lower prices. If an agreement on mutual recognition can't be reached, this value chain will be affected. UK importers will need to develop the logistic facilities to store the produce and southern African exporters will need to certify and eventually comply with two different standards. (For example, less stringent British requirements on 'black spot' will not benefit those producers who need to continue producing under the most stringent EU standards.) This may result in lower variety and higher prices for consumers.

Table 2 maps the current access terms for developing countries to the UK. Even if it is assumed that EPAs would be concluded with the EU and rolled over to UK FTAs, a number of LDCs would suffer: Afghanistan, Bangladesh, Bhutan, Cambodia, Haiti, Laos, Myanmar, Nepal, Somalia, South Sudan, Timor-Leste and Yemen. These countries would, together, lose £288 million annually. In addition, GSP+ beneficiaries – Armenia, Bolivia, Kyrgyzstan, Mongolia and Pakistan – would lose £89 million in payable duties annually. Meanwhile, at least 17 developing countries (probably more) would be excluded if the UK is only willing to provide market access as part of the bilateral FTAs.

Homogeneous standards regarding the EU and conformity assessment

- The UK could consider adopting EU standards and promote a mutual recognition of conformity assessment. Standards and their certification procedures can constitute a major impediment to trade. As the UK leaves the EU, there is a chance that standards applied in the UK and the EU will gradually diverge. For exporters, meeting multiple standards will imply higher production costs. Consumers, on the other hand, will also see higher prices for exclusive standards.
- There would be some benefit for the UK in adopting similar standards to the EU post-Brexit, as the EU will continue to be one of the main destinations for British exports. British consumers would benefit too, as standards compliance and certification costs would constitute a reduced proportion of the price of goods. However, even in this scenario, exports from developing countries would still need to certify their compliance more than once, raising their trade costs.
- Mutual recognition of conformity assessment should be part of the negotiation with the EU. This will reduce the cost of operating value chains involving firms in UK, EU and developing country contexts. In this way, the UK would be able to certify the compliance of EU standards and vice versa, even for products made in developing countries. Consequently, certification costs of existing value chains involving developing countries will not be increased, even after the UK leaves the Single Market.
- Moreover, this mutual recognition should also be proposed in the agreements that the UK may negotiate with third partners. In this way, developing countries will increase their chances of integrating value chains involving the UK and any of its trade partners.

Simplification of tariffs and tax payments

- Although border procedures are simple and waiting times at UK customs are short, exporting to the UK may still be costly for developing countries. On the one

Table 2. Current developing countries market access to the EU

MFN (31)	Standard GSP (13)	GSP+ (8)	EBA (46)		FTA/EPA (57)	
Argentina	Congo, Rep.	Armenia	Afghanistan	Mali	Albania	Kenya
Azerbaijan	Cook Islands	Bolivia	Angola	Mauritania	Algeria	Lebanon
Bahrain	India	Cape Verde	Bangladesh	Mozambique	Antigua and Barbuda	Lesotho
Belarus	Indonesia	Kyrgyzstan	Benin	Myanmar	Bahamas	Madagascar
Bermuda	Micronesia	Mongolia	Burundi (*)	Nepal	Barbados	Mauritius
Brazil	Nauru	Pakistan	Bhutan	Niger	Belize	Mexico
Brunei	Nigeria	Paraguay	Burkina Faso	Rwanda (*)	Bosnia and Herzegovina	Moldova
China	Niue Island	Philippines	Cambodia	Samoa	Botswana	Montenegro
Cuba	Sri Lanka		Central African Republic	São Tomé and Principe	Cameroon	Morocco
Gabon	Syria		Chad	Senegal	Chile	Namibia
Iran	Tajikistan		Comoros	Sierra Leone	Colombia	Nicaragua
Iraq	Uzbekistan		Congo, Dem. Rep.	Solomon Islands	Costa Rica	Occupied Palestinian Territory
Kazakhstan	Viet Nam (*)		Djibouti	Somalia	Dominica	Panama
Korea PDR			Equatorial Guinea	South Sudan	Dominican Republic	Papua New Guinea
Kosovo			Eritrea	Sudan	Ecuador	Peru
Kuwait			Ethiopia	Tanzania (*)	Egypt	Serbia
Libya			Gambia	Timor-Leste	El Salvador	Seychelles
Malaysia			Guinea	Togo	Fiji	South Africa
Maldives			Guinea Bissau	Tuvalu	FYR Macedonia	St Kitts and Nevis
Marshall Islands			Kiribati	Uganda (*)	Georgia	St Vincent and the Grenadines
Oman			Laos	Vanuatu	Ghana	St. Lucia
Palau			Liberia	Yemen	Grenada	Suriname
Qatar			Malawi	Zambia	Guatemala	Swaziland
Russian Federation					Guyana	Trinidad and Tobago
Saudi Arabia					Haiti	Tunisia
Thailand					Honduras	Turkey
Tonga					Ivory Coast	Ukraine
Turkmenistan					Jamaica	Zimbabwe
United Arab Emirates					Jordan	
Uruguay						
Venezuela						

(*) It has negotiated an FTA. Signature or ratification pending.
Source: EU TARIC, http://ec.europa.eu/trade/policy/countries-and-regions/

hand, there are low *de minimis* thresholds that trigger duty payments (i.e. every import above €150 must pay duties). On the other, imports of more than €22 incur VAT (Pope et al., 2014). It will be beneficial for developing countries, as well as tax efficient for the UK, to raise these thresholds immediately after Brexit. To avoid losing revenue and creating unfair competition for domestic suppliers, these benefits should be limited to imports from developing countries, on a strictly business-to-consumer basis, and only for consignments of single or small amounts of units. VAT on these transactions could also be forfeited.

4. The UK should pursue win-win options.

Aid for Trade

Aid for Trade (AfT) develops productive capacities in developing countries and helps developing countries implement trade agreements. ODI research has shown that AfT can reduce transport costs by improving infrastructure and facilitating trade. This benefits the recipients of aid directly by stimulating economic development, which in turn will stimulate imports, with some of these coming from countries that give that aid. This brings an indirect benefit to providers of aid.

There is a further indirect effect insomuch as AfT also reduces the costs of imported products (e.g. garments) which will benefit consumers and processors in countries providing aid. These indirect effects of reduced trade costs offer powerful ways to enhance global welfare. Examining the impact of planned allocations of EU aid between 2014 and 2020 across a range of areas, ODI research has found that the positive effects of EU aid more than offset the initial costs of EU aid, particularly when Aid for Trade reduces trade cost: the €77 billion cost over seven years leads to greater benefits, with a positive net effect on the EU economy of €1–2 billion (Carreras et al., 2016).

In separate but related ODI research, we have uncovered a more general empirical relationship between bilateral aid (all types) and bilateral exports. Untied aid can help to create business, institutional and technological links between donors and recipient countries. In this way, bilateral aid can also lead to increased bilateral exports. Careful econometric analysis for the UK suggests that every pound of UK aid leads to a 22 pence increase in UK exports. Given that the UK provided around £5.1 billion of bilateral aid in 2014, this has led to an increase in UK exports by almost £1.1 billion. Using input-output models, we further estimate that this amount of exports is linked to around 12,000 jobs in the UK. Given the types of exports and industries involved, many of these jobs are low and medium skilled (Mendez-Parra and te Velde, 2016). This further demonstrates the mutual benefits of aid (for full methodology and sources, see Annex 1).

Services preferences

Although access to the UK market for services is quite liberalised, the UK can benefit by providing preferences to developing countries in some services and provision modes. For example, the provision of services by the movement of natural persons, under provision Mode 4, may offer opportunities for small entrepreneurs from developing countries to deliver services in the UK for a period of time. Moreover, seasonal workers from developing countries can provide cost-effective services to British farmers and improve their competitiveness.

Conclusion

The UK is looking to become a leader in the global economy. To a significant extent, this is expected to be achieved through the negotiation of a trade deal with the EU, by rolling over existing trade EU FTAs and negotiating new ones with countries outside the EU, such as Canada, Australia and the US. However, this strategy does not consider the realities of the poorest countries for which the UK remains an important export destination. The consequences of a loss in market access could be very serious for these countries and would also undermine the objectives set out in DFID's Economic Development Strategy.

The UK must implement a dedicated strategy for these countries. This needs to at least roll over existing EBA and GSP+ preferences. However, the UK should also take the opportunity to improve these schemes by simplifying them and sharpening the details contained within them. Finally, in areas such as standards and AfT, the UK should focus its attention on ensuring that Brexit, in addition to being a success for the UK, also contributes to the economic development of the poorest countries. Only by pursuing these win-win strategies can the UK become a real global leader.

Annex 1

Examining the effects of aid on the economy of aid providers*

We examine the effects of bilateral UK aid on UK exports. We do this by using standard econometric techniques (i.e. a gravity model that uses data on 180 countries from 1989-2014) which explain the variation in bilateral export patterns by a number of variables. These include incomes in the UK and its partners, distance between the UK and its partners, cultural and historical links, trade policy (e.g. tariffs applied in the recipient countries) and bilateral aid.

We calculate a positive effect of £1.1 billion in additional UK exports. This is explained by the fact that aid may contribute to technological, institutional and business links between the UK and its partners. For example, there might be 'goodwill' towards donor exporters or the existence of trade concessions towards donors' exports (Arvin and Baum, 1997; Arvin and Choudry, 1997; Arvin et al., 2000). Moreover, aid could also be regarded as an export-promoting activity, for example, through the presence in the recipient country of an embassy or consulate and the organisation of trade missions or conferences (Moons and van Bergeik, 2011).

Whilst the gravity models we used are based on aggregate data, we also consider how different UK export sectors are likely to be affected. We calculate the value of output required from each sector to match the increases in export demand by using input-output tables for the UK economy. Finally, we obtain the number of 12,000 jobs created by applying the labour coefficients in input-output table to the sectoral output calculated.

Data are from standard databases. Aid disbursements are taken from the Organisation for Economic Co-operation and Development (OECD) Development Financial Statistics. Trade data are taken from the EU ComExt database. Control variables used in the regressions are taken from the World Bank World Development Indicators (WDI), the Centre d'Études Prospectives et d'Informations Internationales (CEPII), tariff data for the recipient countries were obtained from the UN Conference on Trade and Development (UNCTAD) Trade Analysis Information System (TRAINS) database. Input-output tables from the World Input Output Database (WIOD) (Timmer et al, 2014).

* For further details, see (Mendez-Parra and te Velde, 2016).

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