HOW WOULD BREXIT AFFECT RETAIL?

March 2016

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FOREWORD

The question of the UK's membership of the EU will be a defining political and economic issue for the foreseeable future. No Member State has ever left the EU and there is no precedent to help assess the wider macroeconomic implications of leaving[1].

The Prime Minister signalled the start of the referendum campaign when he announced the terms of the UK's new settlement with the EU on 19 February. These terms will now be put to the British people in a referendum on 23 June.

In the run up to the agreement on 19 February, the BRC wrote to the Government to encourage it to prioritise the competitiveness agenda in its requests for a new settlement. The Government took heed and it is encouraging that the agreement with the EU says the right things about the importance of free and open markets in Europe and further afield, and also about the importance of sound regulatory frameworks. We shall continue to press the Government and the EU to turn good intentions into concrete action.

In the meantime, it is clear that there is an appetite from all interested parties for more information about the Brexit debate and what it means for people and for businesses. Our aim is to respond to this need by providing our members with as much factual information as possible in order for them to reach their own conclusions about Brexit. How Would Brexit Affect Retail? is our contribution to this very important discussion in the run-up to the referendum.

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Chief Executive
BRC

Spring 2016

1 Greenland did leave the EU in 1985, but for a variety of reasons cannot be considered to be a useful precedent.

EXECUTIVE SUMMARY

Following the outcome of the UK Government's negotiations on EU reform, it is up to the British people to come to a conclusion about whether they believe the UK would be better off staying within the EU or leaving it entirely.

While there will be many aspects to each individual's decision making, we can see that continued access to the Single Market is critically important for retail because so much of the UK's trade is with the rest of the EU and it means that UK retailers can import and export products at the best prices with the minimum of red tape (customs procedures and restrictions). Leaving the EU but remaining in the Single Market would require the UK to be subject to EU legislation without any formal role in deciding it.

However, leaving the EU but remaining in the Single Market is not straightforward politically because it would require that the UK's borders remain completely open to workers from other EU countries.

International trade is becoming increasingly important for the UK. The EU needs to demonstrate that it can deliver trade liberalising agreements with our main international trading partners that would be at least the same, if not better, than agreements that the UK could strike on its own.

There are very legitimate concerns about the amount and quality of regulation that issues from Brussels and it is sometimes assumed that leaving the EU will mean less regulation on business. However, that overlooks the fact that successive UK governments, independently of the EU, have a track record of producing burdensome and complicated legislation and regulation for retailers.

The view of individual retailers on the UK's membership of the EU will ultimately depend on their assessment of whether staying in a reformed EU or leaving it will provide better access to competitive retail markets in Europe and elsewhere, and access to the widest range of sustainable products to meet the demands of consumers globally.

READY RECKONER

LEAVE THE EU ENTIRELY	LEAVE THE EU, STAY IN THE SINGLE MARKET
IMPORTS • **Imports from the EU would be more expensive and delivery times would be extended.** Scale of increase would vary from product to product, but could range from 1-2% up to an extra 15% for textiles and clothing. • **Duty rates on imports from outside the EU would be largely unaffected in the short term.** Over time duty rates would probably come down if the UK negotiated new trade deals. • **Opportunity to source food products** currently banned for "health and safety" reasons from the EU.	IMPORTS • **No change in costs of importing from EU**, except for food, which probably would not be covered by any deal to keep the UK in the Single Market. • **Food imports from the EU could become considerably more expensive** because customs duties would be applied to trade in food between the EU and the UK. • **Duty rates on imports from outside the EU would be largely unaffected.** Over time duty rates may come down. • **Opportunity to source food products** currently banned for "health and safety" reasons from the EU.
EXPORTS • **Higher value e-commerce sales to the EU would be more expensive** and would take longer to deliver. • **Exports to non-EU countries would be unaffected.**	EXPORTS • **E-commerce exports to the EU and beyond would be unaffected.**
INVESTMENT • **No change in the UK** – HMG unlikely to introduce new restrictions on FDI in retail. • **EU host countries hostile to FDI** would find it easier to block retail investment from the UK as the UK would not be protected by the Services Directive and the Commission would have no reason to challenge Member States who applied restrictive practices.	INVESTMENT • **No change**
RED TAPE • **EU rules would still apply unless and until they are withdrawn by HMG.** • **New national rules on product standards could increase production costs** if they require significant changes to manufacturing processes.	RED TAPE • **UK would be bound by all EU legislation related to the Single Market**, but would have no say in the development and agreement of new rules.
GOVERNANCE • **UK would immediately regain sovereignty over all its laws**, however EU legislation that has been transposed into UK law (i.e. most EU regulation) would still apply until repealed. • **Lighter touch UK laws may reduce costs** and administrative burdens. On the other hand, **different UK standards for products would lead to higher sourcing costs.** • **UK would save around £8 billion** net payments to the EU. • **UK government might also "save" money if it reduces the amount of support it pays to farmers**, although there is a risk that farmers might seek to compensate for any reduction in financial support from the government by passing on higher prices along the supply chain.	GOVERNANCE • **The UK would continue to be bound by EU law**, but would have no way of influencing this law because it would have no Commissioner, no MEPs and no representative on the Council. • The UK would be required to **make bilateral payments to other less well-off EU member states** as part of the price of access to the Single Market. **These payments are likely to be at least €1-2 billion per year.**
PEOPLE AND LABOUR • **UK would be able to restrict immigration from EU and elsewhere.** • Likely to impact retail less than some other industries as only 4-5% of jobs are held by EU nationals.	PEOPLE AND LABOUR • **The UK would not be able to restrict the free movement of labour from elsewhere in the EU.**

TRADE

IF THE UK LEFT THE EU, COULD WE TRADE MORE FREELY?

In principle, the UK would be free to set its own trade policy if it was no longer a member of the EU. In practice, this means that the UK could decide on what level to set customs duties for imports and decide what products to restrict for health and safety reasons (particularly important for agricultural products). Critically, the UK could seek to negotiate trade agreements with other countries. However, this does not mean the UK would have an entirely totally free hand.

World Trade Organisation (WTO) rules would make it difficult for the UK to raise import restrictions above the current level[2] applied by the EU. WTO rules would also require that the UK has a clear framework in place[3].

IF WE LEFT THE EU, WHAT WOULD BE THE UK'S TRADE POLICY?

WTO rules would not allow a regulatory vacuum and so some form of regulatory framework would be needed. This would include a nomenclature for classifying products, a schedule of import duties and restrictions, a methodology for determining the origin of products and a methodology for calculating the value of imports.

Since trade policy and customs regulation is a very complex area, it is possible that a UK government would take a pragmatic decision in the short term to simply adopt the EU's trade policy (i.e. the one that it already applies) as its own upon leaving the EU. It would be attractive for traders to do this because adopting the EU's trade regime would minimise disruption and uncertainty for them. There would also be attractions for the Government because maintaining existing customs duties and other restrictions could provide negotiating capital for future bilateral trade deals.

IF THE UK LEFT THE EU BUT BORROWED THE EU'S TRADE POLICY FOR THE SHORT TERM, WHAT WOULD HAPPEN TO IMPORTS FROM OUTSIDE THE EU?

If we assume that in the short term the UK pragmatically adopts the EU's trade regime there would be no impact on the price or availability of imports from outside the EU.

AND WHAT ABOUT IMPORTS FROM INSIDE THE EU?

If the UK left the EU but remained part of the Single Market, importers of goods from the EU would see no change in price and availability for non-food products. However, the situation, is very different for food. Food imported from the EU could become very much more expensive, because access to the Single Market for food depends upon compliance with the CAP, and the UK would almost certainly leave the CAP if it voted to leave the EU.

If the UK left the EU and the Single Market and negotiated an across-the-board free trade agreement with the EU, there would be a marginal increase in the cost of importing to the UK as a result of the reintroduction of customs procedures. This might or might not be passed onto customers.

2 Technically, the relevant maximum rate would be the "bound" rate notified to the WTO, but it is too detailed a point for this paper.

3 The UK would need systems for classifying imports, establishing the origin of imports, defining customs duty rates and any quantitative restrictions, defining import restrictions for health, safety, environmental reasons and public interest reasons.

If the UK left the EU without negotiating any trade deal with the EU, imports from the EU would additionally be subject to Most Favoured Nation (MFN) duty rates. For certain non-food products MFN duty rates are quite high[4] and even higher for food imports. Additional costs at this level would even more likely be reflected in higher prices.

WHAT WOULD TRADE AGREEMENTS LOOK LIKE IF WE DIDN'T STAY PART OF THE SINGLE MARKET?

The UK would almost certainly want to negotiate preferential trade agreements with other countries if it did not remain part of the Single Market over the medium to long term, including the EU.

Views differ on how successful the UK might be in this. Some argue that outside the EU the UK would lack negotiating clout, and would either not be able to attract partners to negotiate with or would end up with one-sided deals that favoured larger partners at the expense of the UK. Others argue that the UK is instinctively open in its approach to trade and would be able to reach more liberal trading agreements with partners, because it would not disrupt the negotiations by trying to protect inefficient domestic industries.

There is merit in both views. As a smaller economy, the UK may have some difficulty in persuading others to invest resource in negotiating a trade deal. However, once an agreement to negotiate had been reached, it is likely that the UK would be far less defensive in its position than the EU has been. In turn, negotiating partners may be willing to be more open to the UK, leading to more ambitious trade deals, negotiated more quickly.

WOULD A UK OUTSIDE THE EU BE ABLE TO REMOVE BARRIERS TO IMPORTS?

In theory, an independent UK would be free to reduce or remove barriers to imports unilaterally. It would not have to negotiate this with anyone, and as an open, trading nation, there would be some in the UK advocating a very liberal import policy. On the other hand, others will argue that for the short term, it is important to maintain the existing level of tariff protection, in order to give the UK Government "negotiating capital" for any talks it opens on free trade agreements with other countries.

Overall, whether it is through negotiations or through liberalisation, there would be considerable scope for the UK to reduce over time the cost of imports from outside the EU and extend the variety of products it can import.

This is particularly true for food where existing duty rates are high and there is a range of restrictions on products for health and safety reasons. The UK farming lobby would argue vigorously against reducing import barriers to foreign food and there would be a wider political issue about opening the UK market to foods that had previously been perceived to have not met our health and safety standards. Nevertheless, the fact remains that outside the EU, there would be an opportunity to reduce the cost of food imports and increase their variety.

4 Around 12 per cent for many textiles and clothing products.

SHOULD THE UK TRY TO STAY IN THE SINGLE MARKET?

The EU remains the single largest market for UK exports[5] and the UK already has the best possible trade terms with other EU member states as a result of the Single Market[6]. For the UK to maintain its existing level of access to other EU export markets and (vice versa) it would need to remain part of the Single Market.

There are pros and cons to EU membership, but the most unambiguously useful part of the EU is the Single Market. Access to the Single Market remains the retail industry's top EU priority.

The benefits of the Single Market are most evident for retailers when they import goods from the EU. However, there are other aspects to the Single Market which can benefit retailers. Access to the Single Market would give some marginal advantages to cross-border e-commerce exporters, but only for higher value transactions. In addition, access for UK retail investments to other EU markets should be ensured in the Single Market (although experience suggests that this protection is of limited value).

The Single Market has delivered benefits but it is far from complete. That is why the BRC pressed the Government to include demands for strengthening the Single Market in its EU renegotiations. The "new settlement" for the UK in the EU responds to those demands with some encouraging words, although these need to be translated into concrete actions.

WHAT WOULD HAPPEN TO EXPORTS IF THE UK LEFT THE SINGLE MARKET?

If the UK did not continue to be part of the Single Market, then it should seek to negotiate a free trade agreement (FTA) with the EU. However, even a comprehensive FTA without customs duties or quantitative restrictions, would not offer terms of access to the EU which are as beneficial. This is because it would involve the reintroduction of customs formalities and procedures which are estimated typically to add costs equivalent to at least 2% of the value of consignments[7].

The worst outcome for UK exports would be that the UK leaves the EU and the EU imposes MFN terms on imports from the UK. This would mean the introduction of customs formalities; procedures and duties on exports from the UK to the EU on a wide range of products, especially food.

The introduction of restrictions and customs duties on EU imports from the UK could affect UK retailers in two ways.

B2C e-commerce sales from the UK would be subject to customs controls adding to delivery times and costs. However, individual consignments with a value of less than €150 would still be exempt from customs duties.

B2B transactions where retailers supply goods from the UK to retail operations in the EU (their own or others) would be subject to the full applicable rates of duty in the EU.

5 54.8 per cent of UK exports went to the EU in 1999 compared with 44.6 per cent in 2014. ONS – How important is the EU to UK trade and investment?

6 There are no customs duties or quantitative restrictions on trade between Member States. Nor are there any customs procedures or formalities.

7 WTO Information Centre: Trade Facilitation

PRICES

IF WE LEFT THE EU WOULD FOOD BE CHEAPER?

In the long term, if the UK left the EU there would be an opportunity to source a wider variety of food products at lower prices from outside the EU. For this to happen, the UK would need to reduce or remove the current tariff barriers to imports and remove some of the restrictions in place for public health, environmental or public interest reasons. At present these barriers are high[8].

The price of imported food from inside the EU would almost certainly become more expensive, even if the UK stays in the Single Market, because a Single Market agreement would not cover trade in food. The precise impact on food prices would depend upon what tariff rates are put in place on imports, but the worst case would see the application of MFN rates that could almost double the import price of products like beef, cheddar cheese and wheat flour.

IF WE LEFT THE EU WHAT WOULD HAPPEN TO DOMESTIC FOOD PRODUCTION AND UK FARMING?

Domestically produced food may become more expensive as farmers seek to compensate for any loss of subsidies as a result of exiting the CAP by forcing price increases through the supply chain. In extreme cases, if the UK Government does not substantially replicate the support available through the CAP, the viability of some domestic production could be threatened, throwing into question the strategies developed by many retailers to promote local and national sourcing of food.

Over the longer term, exposure to competition from outside the EU and a removal of agricultural subsidies could provide the impetus for greater efficiency and competitiveness in the UK farming sector[9].

WHAT WOULD HAPPEN TO THE CAP?

At present, UK farming receives around £3 billion in subsidies under the Common Agricultural Policy (CAP). Leaving the EU would almost certainly mean leaving the CAP. The farmers would understandably push the UK Government for some form of support to replace CAP payments, and it is unlikely that the UK would simply withdraw support completely from the industry.

On the other hand, given its approach to spending in other areas, it is unlikely that any national support measures for farming in the UK would be as extensive or generous as those enjoyed under the CAP, at least in the medium to long term. Farmers might well seek to recoup the loss of income from subsidy payments through higher prices for their products.

8 Imports of beef carcasses from outside the EU attract customs duties of 12.8 per cent of the value of the consignment plus €1,768 per tonne.

9 Following substantial industry restructure, New Zealand now exports 80 per cent of its beef production and 92 per cent of lamb production.

RED TAPE AND REGULATION

Overall, it is undoubtedly true that a UK outside the EU would have far more control over legislation governing many aspects of retail operations (though the cost of continued access to the Single Market would be the continued application of significant amounts of EU legislation). However, the evidence does not support the argument that by leaving the EU, British business (and retail in particular) would enjoy a more benign regulatory environment.

WOULD THE UK BE FREE OF RED TAPE OUTSIDE OF THE EU?

If the UK remained in the Single Market, it would continue to be bound by a raft of EU laws over which it would have absolutely no influence. Of particular interest to retailers, this would include product regulation and information requirements, for example the Food Information Regulation.

Manufactured products and other services would still need to comply with the relevant legislation in export markets in order to be legally marketed there. Despite the claims of successive governments, the UK has a track record in introducing its own burdensome regulation. The UK and its devolved administrations have introduced legislation that has increased the costs of UK retail business without any compulsion from the EU[10].

HOW MUCH RED TAPE ACTUALLY COMES FROM THE EU AND CAN WE GET RID OF IT ANYWAY?

Estimates of how much legislation actually originates in Brussels vary[11]. In many areas the UK has actually gone beyond EU requirements.

Leaving the EU does not necessarily mean losing the burden of EU regulation because most of this has been enacted now as UK law and will still apply unless and until it is specifically withdrawn by the UK Government.

10 Additional legislation includes: GSCOP and the Adjudicator; retail specific levies and charges in Scotland and Northern Ireland, carrier bag charging; increased penalties for restricted sales; tobacco display bans; consumer guarantees; unfair contract terms.

11 From a retail perspective it is probably more helpful to list the relevant legislation that comes from Brussels: all trade and Single Market legislation, including the right to invest and operate in other European countries; virtually all food product labeling requirements; some aspects of consumer law; many aspects of weights and measures regulation; 80 per cent of non-food product safety legislation; the majority of health and safety legislation; environment and emission legislation, including waste and recycling and much labour market legislation. In addition the EC has significant powers to investigate and enforce competition rules.

INVESTMENT

WOULD THE UK OUTSIDE THE EU ATTRACT MORE INVESTMENT?

The UK is already the destination of more foreign direct investment (FDI) than any other EU member state and in 2013 accounted for as much retail FDI as the rest of Western Europe put together[12].

Continuing investment in the UK retail market is more likely to be driven by the continuing vibrancy of the market in the UK rather than because the UK is in or out of the EU.

More widely, many companies investing in the UK, especially in manufacturing, have done so because the UK is the best option for them to access the wider EU market. Outside of the EU, and in particular outside of the Single Market, there would be less rationale for the UK as a centre for supplying Europe.

It is difficult to see how the UK would become a more attractive destination for FDI if it left the EU and had less access to EU markets, and the introduction of tariff barriers could mean investors go elsewhere. On the other hand, a lighter regulatory regime in an independent UK may compensate for the increased barriers to trade with other member states but this cannot be taken for granted.

WHAT WOULD HAPPEN TO UK RETAIL INVESTMENT ABROAD?

It is worth considering whether leaving the EU would have implications for UK retailers looking to establish elsewhere.

In relation to markets outside the EU, there would probably be very little difference because generally speaking membership of the EU does not confer any particular benefits for UK retail investors in third countries.

In theory, the situation is different within the EU, where the Services Directive should guarantee that UK retailers can establish themselves in other EU markets as easily as domestic retailers. The steady stream of complaints about discriminatory practices from other EU Member States, in particular those in Central and Eastern Europe, suggest this is not the case.

12 The World Shopping Capitals 2011 survey found that, of the 22 major cities surveyed, London was the world's shopping capital, coming in at number 1 for all three of the categories surveyed: largest total retail sales (food and non-food) £91.9 billion; largest non-food retail sales £64.2 billion; largest online sales £9.9 billion.

THE LABOUR MARKET

WOULD CONTROL OF UK BORDERS MEAN MORE JOBS AND BETTER WAGES FOR BRITISH WORKERS?

The effect of labour migration from the EU on jobs and wages in the UK is one of the most contentious issues in the EU membership debate, but remains inconclusive[13].

The retail industry has relatively low exposure to migrant labour from elsewhere in the EU. Around four per cent of retail jobs are accounted for by EU nationals, compared with an average of five per cent for all industries and nine per cent for accommodation and food services. The impact on wage rates and jobs arising from a reduction in the availability of labour from elsewhere in the EU is likely to be less pronounced in retail than in other industries, including some in the retail supply chain such as agriculture.

Ironically, the likely price for the UK's continued participation in the Single Market would be continued free access to the UK labour market from elsewhere in the EU. A condition of Norway's participation in the Single Market is that it keeps its borders open to workers from the EU but that the EU remains open to Norwegian workers. Norway currently experiences far higher per capita rates of migration from elsewhere in the EU than the UK does.

SAVING THE UK MONEY

WOULD WE SAVE MONEY IF THE UK LEFT THE EU?

Our net spending on the EU equals a little over one per cent of total government expenditure. In 2018 HM Treasury estimates the UK's net contribution will be £8 billion (HMT European Union Finances 2013).

In 2013, the UK paid just over £17 billion to the EU. After the UK's rebates and receipts (e.g. CAP payments to UK farmers) the net total was £8.6 billion.

The UK is second largest net contributor to the EU budget behind Germany.

If the UK left the EU it could certainly save £8 billion per year net payments, although if it remained in the Single Market it would have to make payments to less developed Member States of at least £2 billion, perhaps more. Outside the EU, UK Exchequer could also make significant further savings of up to £3 billion each year if it chose not to introduce a system of agricultural support to replace the CAP. In this case, retailers and others in the food supply chain may face pressure from farmers to compensate for the loss of that income. That pressure would probably take the form of higher prices in the market.

13 'There is no widely accepted estimate of the effects of immigration on employment, output, or any other economic indicators. Most studies on the impact of migration on the UK economy have found weak or ambiguous effects on economic output, employment and wages. A few studies, however, show some displacement of resident employment in low-skilled jobs.' House of Commons Leaving the EU 1 July 2013.

TIMEFRAME

HOW QUICKLY COULD THE UK BE FREE FROM THE EU?

The referendum on the UK's membership of the EU has been set for 23 June.

In the event of vote supporting exit, the UK Government would invoke Article 50 of the Treaty of Europe.

An exit from the EU would take a minimum of two years using the process set out in Article 50 of the Treaty of Europe, which sets out the rules for a country leaving the EU. Nothing changes until the final agreement is made including the rules that govern trade between the UK and the EU and the rest of the world. Formally, the UK would not be involved in negotiations, although it is likely that in the event of a vote for Brexit, the UK would work very closely, albeit informally, with the EU to agree the terms of exit.

Upon leaving the EU, the UK could immediately seek to negotiate new trade deals with partners. These would be likely to take longer if the negotiations were wide-ranging (e.g. including investment rules, regulatory co-operation) and shorter if they concentrated on purely trade issues (i.e. customs duties and other import restrictions).

In any case, the minimum credible period for negotiating a bilateral trade deal is two years (and often considerably longer). It is unlikely that the UK would have the capacity to negotiate bilateral trade agreements simultaneously with all its significant trading partners and so new bilateral negotiations would probably be staggered over a period of years[14].

The situation would be different for UK imports, where the UK could act more quickly. WTO rules would allow the UK government to unilaterally lower its tariffs and duties as soon as it left the EU. This would require no negotiation and could be applied immediately. WTO rules would make it far more difficult for the UK to raise import barriers beyond their existing level.

14 Of the UK's top 20 export destinations about half are in the EU and half outside. A single trade negotiation would suffice for those countries in the EU but separate negotiations would be required for the rest. Assuming a maximum of 5 negotiations at a time, the minimum period it would take to establish preferential access for UK exports to its 20 biggest export markets would be 4-5 years.

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