Article 50 has been triggered
What are the Trade implications for Irish businesses?

Yesterday, the British government formally triggered Article 50 of the Lisbon Treaty which officially launched the two-year negotiating process that the UK will undertake as it leaves the EU. Britain's departure and its future relationship with the EU is bound to have profound economic and trade ramifications for businesses globally, throughout Europe and in particular Ireland. Implications such as;

- Tariffs arising between Ireland and the UK
- Custom controls on the island of Ireland
- Increased administrative costs
- Reduced UK demand & predictability of demand
- Decreased domestic demand for Irish goods and services
- Increased Irish unemployment
- Exchange rate volatility

European Customs Union

Prime Minister Theresa May has been clear that the UK will leave the EU Customs Union so that it can go out and strike its own trade deals with other countries. As such, Britain will no longer abide by the Common External Tariff (CET) which will result in custom controls and border checks between the Republic and Northern Ireland.

An inevitable return to a Hard Border

All EU member states are subject to the CET which is enforced along the EU's external border. The enforcement of the CET means that internal controls within the member states are no longer necessary and trade deflection is avoided. With the UK leaving the Customs Union and thus free to apply its own external tariffs, a hard border on the island of Ireland is unavoidable, even if a Free Trade Agreement is agreed between the EU and UK. Why? Take the scenario below;

- An FTA is established between the EU and Britain
- The UK sets a tariff on Japanese cars of 20%
- The EU currently has a tariff on Japanese cars of 10%
- Without border controls, trade deflection would arise as Japanese cars would be imported into the UK via the EU
- This would undermine the UK's trade policy, making it obsolete
- So long as the UK and the EU set different tariffs, there will be border controls between both jurisdictions, including between the Republic and Northern Ireland

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Irish businesses will have to prepare for the reality of a reintroduction of a border with Northern Ireland and react accordingly. Many firms have yet to face this inevitability, relying on statements by Irish and UK politicians that there will be no return to a hard border and that any kind of border will be ''seamless as possible'. Complacency of this sort extremely risky.

Even if it were possible for Ireland not to impose border checks with the North and yet remain inside the EU, the result would be equally damaging. This kind of scenario would mean Ireland was in effect outside the Customs Union and thus trade between Ireland and the EU26 would necessarily be subject to costly border and customs formalities, so as to rule out trade deflection.

Britain's decision to leave the European Customs Union will result in border checks and custom controls returning to the island of Ireland. Irish businesses must react and prepare now.

Costs to Irish businesses

When Britain leaves the EU, customs controls will be reintroduced for imports from and exports to the UK. From a trading perspective, the UK will become a third country which means the regulatory framework for trade with countries outside the EU will be applicable in full. Large multinationals will likely already have knowledge of this regulatory framework while indigenous Irish SMEs that only trade with the UK will now have to adjust to meet the costly demands of trading with a third country.

- New administrative costs
- Filing export declarations
- Completing commodity codes
- 'Rules of origin' compliance
- Entry summary declarations
- Custom duty's
- Import VAT
- Export licenses

With the prospect of the UK joining the European Economic Area (EEA) ruled out, the only conceivable result will be Britain trading with the EU either through a FTA or on WTO terms. As seen below, both scenarios are enormously costly for Irish businesses

Impact of Brexit on Ireland after 10 years, change from baseline	FTA	WTO
Percent deviation from Baseline Level:		
Exports of goods and services	-3.5	-4.9
Gross value added at basic prices	-2.7	-3.8
Gross value added at basic prices, Traded sector	-3.0	-4.3
Gross value added at basic prices, non-Traded sector	-2.7	-3.6
Personal consumption of goods and services	-2.5	-3.4
Average wage €	-2.5	.3.6
Deviation from Baseline	**FTA**	**WTO**
Personal consumption deflator	-0.2	-0.3
Unemployment rate	1.4	1.9
GDP Deflator	-0.2	-0.3

*ESRI

The figures above paint a challenging picture for Irish businesses. Export levels may decline considerably, the economy is likely to shrink, the rate of unemployment will rise and domestic demand for goods and services will fall. The worst case scenario for Ireland will be the UK crashing out of negotiations on WTO terms which will result in tariffs being imposed on sectors that most heavily depend on Ireland-UK trade. This has potentially disastrous effects for many industries, but above all the Irish agri-food sector.

Irish Agri-food

Sector	Current average tariffs for EU exporters (weighted %)	% of Irish-agri food exports destined for UK 2013-15
Dairy Produce	39.9%	46%
Meat	32.3%	44%
Preparations of meat or fish	31.8%	78%
Sugars and sugar confectionary	30.2%	35%
Waste from food industries & animal fodder	18.4%	78%
Vegetables	15.1%	97%

Trade for the Irish Agri-Food sector will be greatly impacted by Brexit and it will undergo significant change. Research from Teagasc estimates that from a base scenario, 21.5% of UK exports will be diverted and the size of the discount will be 15%. The smallest impact that Brexit will have on the agri-good export value will be an annual loss of €150m or 1.4% while the largest potential impact will be €800m or 8%.

Global Trade Implications

Exchange rate volatility

In the aftermath of the referendum in June 2016, there was been a rapid weakening of Sterling. Negotiations and trade developments over the next 24 months will pose a further significant weakening to the pound against both the dollar and the euro. This current change in currency value is structural not cyclical meaning things could get worse.

For Irish agri-food business

- A 1% weakness in Sterling results in a 0.7% drop in Irish exports to the UK
- A further weakening towards the £0.90 mark would translate to losses of over €700m in food export
- This would translate to losses of over €700 million in food exports and about 7,500 Irish jobs

For US Companies

- A weakening Sterling against an increasingly stronger US dollar results in reduced demand for US exports

- Between the date of the referendum and February 2017, Sterling had fallen by around 16% against the US dollar

Global companies based in UK

International firms with operations in Britain relied on the country's EU membership for free trade access to the European single market and its consumer market of over 450 million people. The UK's exit and the prospect of trade barriers being erected has caused many firms to prepare contingency relocation plans to the remaining EU27. WTO tariffs, supply-chain disruption, custom controls, movement of labour, data protection, diverging regulation and intellectual property implications are now all major concerns for international companies that operate in and from the UK.

International Automobile sector

If negotiations do falter and the EU-UK trade does fall under WTO terms then global firms exporting to the EU from the UK could be hit with high tariffs, particularly industries such as the automobile sector which has complex cross border supply chains and is widely exposed to the EU market. Britain is home to numerous leading global car manufacturers such as Ford, Toyota and Nissan and all have highlighted the risk that Brexit poses to their industry.

The sector in the UK is hugely integrated with its European counterparts and the introduction of WTO tariffs, which range from 2.5%-4.5% for car parts to 10% for cars themselves, could increase the cost of assembling a car in the UK by £2,370. For leading automobile companies based in the UK that export over 200,000 cars a year, this could drive up costs by more than £920m after only two years.

Implications on UK-based financial services

London has long been a global financial hub, hosting the world's leading corporate and investment banking services and acting as a platform to the EU27 through the European Passport System. Now that the UK has triggered Article 50 and will begin its exit process from the EU, it will almost certainly mean that UK-based financial firms will lose their passporting rights which allow them to do direct business with their EU27 clients.

As a result of this, it is estimated that some 35% of wholesale market activities might migrate from London to other major cities in the EU such as Dublin, Frankfurt, Amsterdam and Paris. This could see up to 30,000 people relocating from London to the remaining EU27, a breakdown of 10,000 related to core wholesale banking and 18,000-20,000 related to professional services. However, London will retain a considerable presence of financial services due to its capacity. The UK financial sector trade balance, to which London contributes the biggest share, is greater than that of Ireland, Germany, Amsterdam and France by a factor of more than 10.

This is not to disguise the enormous ramifications that Brexit will have on UK-based financial firms. A wide range of banking actives are covered by the passport such as;

- Deposit taking
- Derivatives trading
- Loan and bond underwriting
- Portfolio management
- Payment services
- Insurance and mortgage brokering

Background context of WTO and tariffs

The World Trade Organization was established on the 1st January 1995 and replaced its predecessor the General Agreement on Tariffs and Trade (GATT) which itself first commenced in 1948. It is an international organization that deals with the rules and regulations of trade between the participating countries by proving a framework by which trade agreements can be negotiated and disputes that arise between nations can be resolved.

The objective of the WTO is to create a global trading system that is non-discriminatory, free from barriers, predictable, more competitive and beneficial for less developed countries. Throughout the several negotiation rounds of the WTO, tariffs have been continuously cut but still remain for many sectors, particularly for agriculture and machinery. Tariffs give a price advantage to locally-produced goods over similar goods which are imported. The latest round of negotiations, the Uruguay Round, committed countries' to cut tariffs and to ''bind'' their customs duty rates to levels which are difficult to raise.

Ever since the Brexit vote last June, the prospect of the UK relying on its WTO membership for access to European & Irish markets has continued to grow. But this is by no means guaranteed and could spell an extensive period of uncertainty for the future trading relationship between the UK and the EU. And for Irish businesses, the longer it takes for Britain to resolve its independent membership of the WTO, the worse it will be:

> *Can the UK immediately trade under WTO terms if it exits the EU with no deal?*
> Most likely yes. The UK is currently a member of the WTO but under the shared membership of the EU, meaning that its ''schedule'' of commitments on agreements covering agriculture, industrial goods and services are presently tied up with the EU's. To minimize disruption and ensure that the UK can trade under WTO terms straight away if such a scenario arises, the minister for International Trade Liam Fox revealed that Britain has prepared the necessary draft schedules which replicated its current obligations.
>
> *Can the UK change its current schedules once out of the EU?*
> Yes it can and it will likely be renegotiated in time, but doing so can take years of extensive consultation and negotiations with the WTO's other 163 members who can object to them.
>
> *What happens if another member objects?*
> If another WTO member does raise an objection or a veto on the UK's attempt to change its schedules, it is only a veto on the certification of the schedules rather than its actual commitments. The certification merely holds evidentiary weight meaning that scheduled commitments still exist even if not certified.

Will the UK want to trade under WTO terms?

Absolutely not, trading under these arrangements would be the ultimate last resort for Britain and be disastrous for its economy, as well as its major trading partners. Despite the fact that Prime Minister May has held the position that no deal is better than a bad deal, such a scenario would see high tariffs being introduced and for a leading trading economy like the UK that is highly integrated in the complex global supply chain, it would cause havoc.

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