



Economic Impacts of Scenarios for Scottish and UK Seafood Industries Post EU Exit

Scottish Government Policy Brief



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Introduction

Scotland's Place in Europe: People, Jobs and Investment, published in January 2018, presents results from Scottish Government analysis of the potential impact of Brexit on Scotland. The analysis examined the long-term impacts of Brexit by comparing potential future scenarios for trade arrangements (all characterised by less economic integration with the EU) to the status quo where the UK is a member of the EU. The results from the economic analysis, presented in Table 1, show that loss of full EU membership will have negative impacts on the performance of Scotland's economy.

Table 1 – Headline Macroeconomic Indicators by 2030 relative to a baseline of full EU Membership

		GDP (%)	GDP Per Capita (£) in 2016 Cash Prices	Real Disposable Income (%)	Business Investment (%)
Trade arrangement	EEA	-2.70%	-£688	-1.40%	-2.90%
	FTA	-6.10%	-£1,610	-7.40%	-7.70%
	WTO	-8.50%	-£2,263	-9.60%	-10.20%

Analysis produced for the Scottish Parliament by the Fraser of Allander Institute (FAI) also suggests comparable negative impacts on the Scottish economy. The FAI analysis shows that failure to agree a preferential trade deal with the EU would, after 10 years, result in:

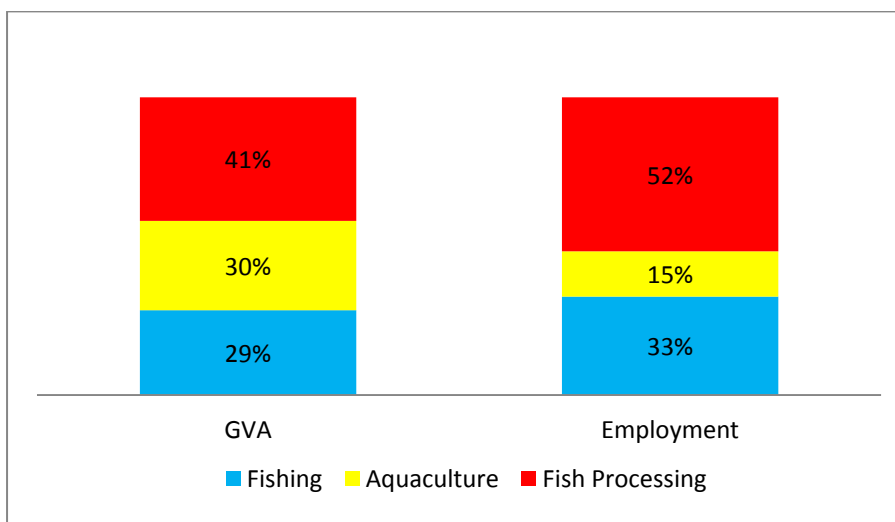
- GDP that is over 5% (£8 billion in 2015-16 terms) lower than would otherwise be the case;
- real wages that are 7% lower, equivalent to a reduction of around £2,000 per year; and
- number of people employed in Scotland that is 3% lower (around 80,000 jobs).

The Scottish Government is keen to understand how these impacts may vary across different parts of the economy, including Scotland's seafood industries.

Scotland's seafood industries – comprising offshore and inshore fishing fleets, aquaculture and onshore fish processing – are important to Scotland. Overall they

account for a relatively small part of Scotland’s economy – 0.17% of Scotland’s gross value added (GVA) in relation to the catching industry and 0.6% of GVA for seafood industries overall, in 2015. That still means, however, that they contributed £733 million in GVA and 14,500 in jobs to the economy in 2015. They are a significant driver for the rural economy in certain localities, often in more remote parts of Scotland. They also do much to contribute to the vibrancy of our coastal communities. Figure 1 shows the distribution of GVA and employment across seafood industries. It shows that fish processing, an onshore activity, creates most value and supports the most employment among seafood industries, with sea fisheries currently contributing the least value to GVA.

Figure 1. Distribution of GVA and Employment for the Seafood Industries, 2015



The Scottish Government’s vision is for sustainable and productive seafood industries which help manage our resources to meet the long-term needs of people, communities and our environment. This requires a future in which all our seafood industries are supported to harness available opportunities to grow sustainably and inclusively – through access to growing markets both at home and abroad, access to labour and skills, adequate financial support to sustain investment, and through maintaining close relationships with other nations to ensure sustainability of shared natural resources and to meet international obligations.

The research, conducted by ABPmer, Interanalysis and Vivid Economics, examines the possible impacts of EU exit on seafood industries, using a range of hypothetical scenarios reflecting changes in three drivers of international trade in seafood: tariffs; non-tariff measures (NTMs) – such as rules of origin and health certification requirements; and production levels as determined by fishing quotas for wild capture fisheries. These are expected to be some, but not all, of the main sources of impacts that could arise from EU exit.

The research has not looked at potential impacts of other drivers for the economic performance of seafood industries, like access to non-UK EEA labour and the grant funding currently available from the European Maritime and Fisheries Fund [EMFF]. Scotland's seafood processing industry relies on non-UK EEA workers for 58% of its labour force (rising to 70% in some areas such as Grampian). The processing industry has already expressed concern that loss of non-UK EEA workers would affect the survival of some businesses. With regard to the EMFF, over the period 2014-2020 Scottish seafood industries and coastal communities will receive up to £150 million in EMFF grant funding and associated match funding.

The loss of funding and/or ready access to labour is likely to result in significant negative impacts on the performance of Scotland's seafood industries, although to varying degrees.

Understanding the report

As with any form of modelling work, assumptions have to be made about possible policy changes, yet there is currently little information available about what those policy changes might be. The continued lack of agreement around the terms of a future relationship with the EU has not made it possible to conduct this modelling on anything but a range of theoretical scenarios; this means we are still some way from being able to test the potential impacts of practical proposals for the UK's exit from the EU. The four sets of scenarios used in the research modelling, therefore, are hypothetical constructs designed to demonstrate and test the sensitivities of seafood production and trade to any possible changes that could arise due to EU exit. They are not an exhaustive list of all possible scenarios. Some of them are more plausible than others. The sets of scenarios examined by the research can be summarised as follows:

- **Scenario 1** – Free trade with EU and rest of the world, and successful renegotiation of total allowable catch (TAC) shares or fish quotas in the UK's favour (from other EU member states) based on zonal attachment principles. This is the least likely or plausible scenario. No state enjoys this level of free trade with all other countries. If the UK was to act as an independent member of the WTO, it could in the future negotiate free trade or preferential trade agreements with a range of key countries that import Scotland's seafood. Without such free trade or preferential trade agreements, the World Trade Organisation's "Most Favoured Nations" (MFN) tariffs would be applied to any trade. Notwithstanding this, this scenario allows the research to explore market opportunities that might be realised outside the EU.

Moreover, it is unlikely, in the immediate future, that the levels of UK fishing quotas will change. However, this scenario assumes, for analytical purposes, the maximum possible TAC shares or fish quotas for the UK, based on one

interpretation of the zonal attachment principle. Achieving these larger fishing quotas will require negotiation with other states, who may not be willing to accept significant changes to TAC shares. The EU has already set out in its negotiating guidelines that if the UK wants to maintain tariff-free trade across all sectors of the economy, current 'TAC' (total allowable catch) shares or fishing quotas will have to apply.

It should be also understood that that the zonal attachment principle may not necessarily be the optimum basis for such renegotiation nor indeed the preferred approach of the Scottish Government to any such renegotiation. Such decisions as to the basis upon which to base policy regarding future management of Scotland's fisheries are yet to be made. This scenario should thus be viewed as very optimistic, and if ever, is unlikely to be achieved on exit or in the short-term.

- **Scenario 2** – an EU-Norway European Economic Area (EEA) type agreement and successful renegotiation of TAC or fish quotas in the UK's favour based on zonal attachment principle. It assumes tariffs on UK–EU trade are similar to those in the current EU–Norway EEA agreement, as well as a modest increase in NTMs between the UK and the EU, and a reallocation of fishing quotas in the UK's favour (as in Scenario 1). It is equivalent to leaving the Common Fisheries Policy (CFP) but staying in the European Single Market through EEA membership, and it most closely reflects the Scottish Government's stated position in the event that we leave the EU. Fisheries and seafood are treated differently under current EEA arrangements, and the UK would not benefit from zero tariffs on all seafood products. As in Scenario 1, the levels of UK fishing quotas in this scenario are highly optimistic.
- **Scenario 3** – No preferential trade agreement with the EU and successful renegotiation of TAC or fish quotas in the UK's favour based on zonal attachment principles. This scenario assumes WTO MFN tariffs apply on bilateral trade between the UK and the EU, together with a larger increase (compared to Scenario 2) in NTMs. This scenario assumes the UK continues to benefit from free trade agreements it enjoys currently as a member of the EU, although clearly this will need to be negotiated. Scenario 3 is slightly less optimistic than Scenario 2.
- **Scenario 4** – No preferential trade agreements with the EU and the rest of the world, and no increases in UK fishing quotas. This scenario assumes no trade deal with the EU and losing access to the free trade agreements that the UK currently enjoys as a member of the EU. This is the worst case scenario, and it broadly represents what is referred to commonly as a no-deal or a hard Brexit.

The research also provides an initial assessment of the potential wider economic impacts of EU exit, including the potential for changes to GVA and employment for Scotland's seafood supply chain.

The research examined the impact of the scenarios on output and trade for 10 seafood species of importance to the UK, based on their share in UK total landings, share in UK export values, importance to the Scottish fleet and potential for quota redistribution under zonal attachment. A successful renegotiation of TAC shares or quotas in UK's favour, based on zonal attachment principles, has potential to increase UK landings for the following quota species covered by the research: cod, haddock, hake, herring, mackerel, Nephrops and saithe. The renegotiation of quotas does not affect non-quota species (e.g., scallops and crab) and aquaculture (farmed salmon, trout and shellfish).

The assumed increases in fish landings in the scenarios is based on a study by University of Aberdeen, which uses one interpretation of the zonal attachment principle. The research has not considered other options for quota allocation or interpretations of the zonal attachment principle. Again, it is important to note that the scenarios are not necessarily the preferred approach of the Scottish Government, which has yet to set out its policy on future management of Scotland's fisheries. The results from modelling these scenarios will be one of the elements used to inform that work.

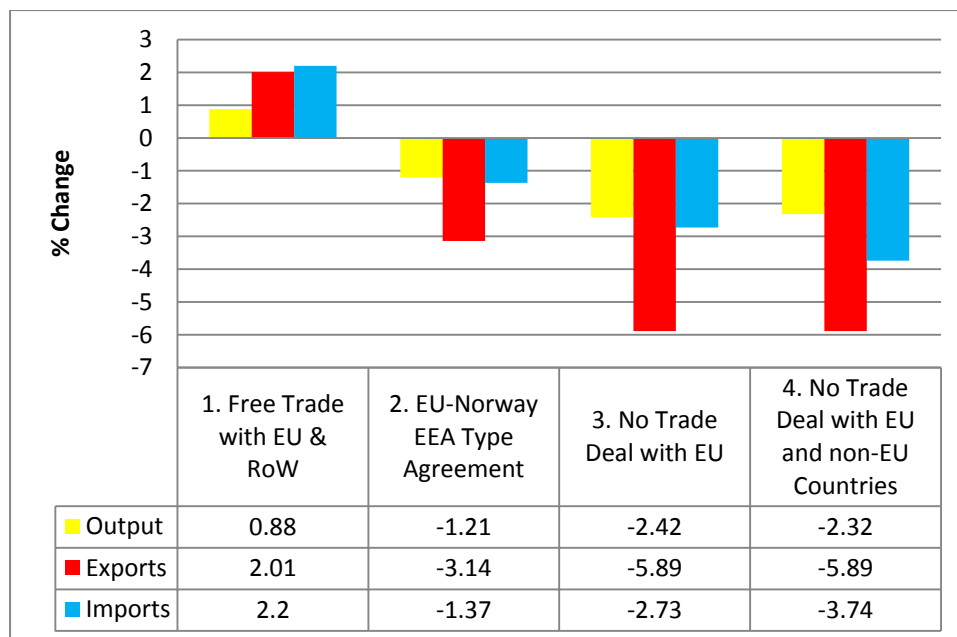
The EU has said in its negotiating guidelines and consistently emphasised that "nothing is agreed until everything is agreed". There is, therefore, the prospect of a transition period commencing after March 2019 but this will not be confirmed until the full withdrawal agreement is reached later this year.

In reality there is unlikely to be any significant change in quota allocations in the short term. Indeed, achieving larger quotas for the UK fleet will take some time to negotiate. On leaving the EU, it might be possible to achieve some quota increases by swapping EU access to UK waters for inward quota transfers, but under current EU27 negotiating guidelines this would mean foregoing tariff free trade with the EU for all sectors of the economy. It is not clear if the UK Government is inclined to accept this trade-off.

Key Findings

Figure 2 presents the impacts of the scenarios on output, exports and imports without increases in fish quotas. It shows that extending free trade to the rest of the world would have a positive impact on trade – UK output, exports and imports would be higher when compared to the 2015 baseline.

Figure 2. Impact of changes to tariffs and NTMs on UK output, exports and imports, % changes from 2015



The introduction of tariffs and higher NTMs on trade with the EU, however, would have a negative impact on trade – UK output, exports and imports would be lower. With current UK shares of EU quotas, the negative impacts of leaving the EU, even whilst remaining within the European Single Market on the same terms as Norway, are still significant. Total output would be lower by up to 7%, depending on the species. Export values would be lower by between 0.9% and 6.6% for the different species, and imports would be lower by up to 5.6%.

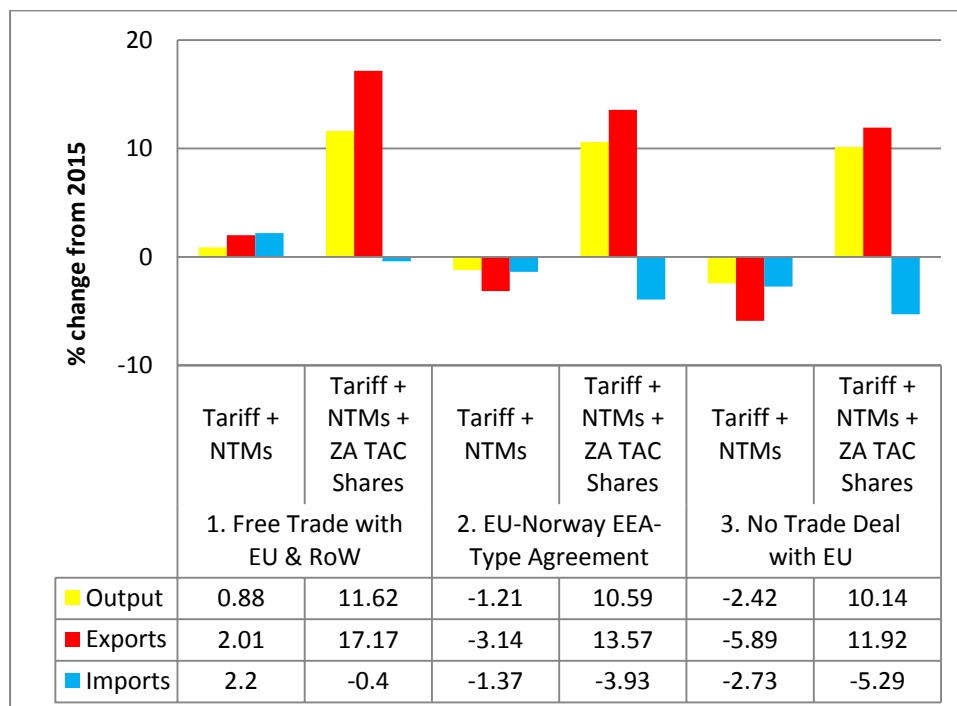
In the absence of larger UK fish quotas, the research findings for Scenario 2 support the Scottish Government’s position that if the UK leaves the EU, then being in the European Single Market offers the least bad alternative for continued access to the EU market. Moreover, it would enable the UK the flexibility to negotiate transfers of quotas in its favour as part of the existing international Coastal States arrangements – as Norway and Faroe Islands already do. The UK may also be able to negotiate, over time, larger TAC shares to reflect better the available resource in UK waters – although as with any negotiation this is not a guaranteed outcome. The results of achieving larger TAC shares are shown in Figure 3).

Scenario 1 sets out hypothetical free trade arrangements with the EU and the rest of the world, where tariffs are removed both for imports and exports, and non-tariff barriers are significantly reduced, which has already been noted is very optimistic and highly implausible. The results for this scenario demonstrate that the preferred outcome for Scotland’s seafood industries (or at least, the fishing sector therein), is to reduce, and where possible, eliminate tariffs and NTMs. That allows seafood

industries to increase their outputs and maintain, or even increase exports. However, with the exception of salmon, mackerel and herring, the expected gains for most species are modest. For these species, the EU remains the biggest market, and the UK already enjoys zero tariffs and very low NTMs on its trade with the EU. It underlines, therefore, that staying in the European Single Market is important for preserving the trade and economic benefits already enjoyed by our seafood industries, including the fishing sector.

These findings also appear to undermine the premise made by the UK Government that there is a world of opportunity that we have not been able to exploit and that by delivering a collection of new trade deals, UK and indeed Scottish businesses will see significant gains. For the seafood industries, we are already maximising our trade opportunities – membership of the EU is not preventing us from accessing major markets such as in the USA and China. Indeed, in some cases it is facilitating access by removing NTMs, as is the case with the USA, where we have mutual recognition arrangements on export health certificates. This arrangement could be lost if we leave the EU, adding further delays and costs to export businesses – in particular the salmon industry, where the USA is one of our major export markets.

Figure 3. Impact of changes to landings (quotas), tariffs and NTMs on UK output, exports and imports, % changes from 2015



Having the opportunity to renegotiate quotas to levels consistent with the zonal attachment principle could over time result in a significant increase in output and exports for quota species. To maximise these opportunities, however, this research highlights the importance of having free access to the EU market. Under the free

trade scenario, the aggregate output for the seafood industries would be higher by 11.6% and exports would be higher by 17.2%. The research estimates that this scenario could result in direct and indirect output levels for Scotland's seafood industries that are higher by up to £540 million, with associated additional jobs and GVA across Scotland's seafood supply chain through direct and indirect impacts.

The benefits of increasing UK quotas to levels implied by zonal attachment, however, are lower under the imposition of tariffs and higher NTMs on trade with the EU and the rest of the world, although most of the losses derives from trade with the EU. The EU has already effectively ruled out the possibility of the UK increasing its quotas and retaining tariff free access to the EU Single Market. This is equivalent to Scenario 3 (MFN tariffs with the EU and high NTMs), where output levels – with zonal attachment shares – would be higher by only 10.1% and exports by only 11.9%. These increases in output and exports are smaller when compared to the free trade scenario. Thus, for any given TAC sharing arrangement, the preferred outcome for the UK seafood industries on leaving the EU would be zero tariffs and the minimum possible NTMs with the EU and the rest of the world.

It should also be recognised that the benefits of increasing Scottish quotas are not shared across all seafood industries. Adjustment of UK quota will not benefit businesses relying on non-quota species, and very specifically the aquaculture industry, which is our largest food exporter. This is important if increasing UK quotas is seen purely in terms of offsetting the costs of tariffs and NTMs. Aquaculture businesses and those focused on non-quota species would have no relief from costs arising from increases in tariffs and NTMs.

Any beneficial impact of increased quotas depends also on capacity to take advantage of these. Capacity would need to build up to take full advantage of any increases in fishing opportunities. A concerted programme of investment may be needed, in particular in onshore processing facilities. Building an internationally competitive onshore seafood supply chain in Scotland could, however, be challenging with EU exit due to the industry's heavy dependence on non-UK EEA labour in the processing industry, which is likely to be reduced if migration from the EU is constrained. Once again, this demonstrates that remaining in the European Single Market and a Customs Union with the EU, with freedom of movement of labour, will be vital to take full advantage of any opportunities which might arise from leaving the CFP.

The research suggests that increases in tariffs and costs linked to NTMs would have negative impacts on farmed salmon output and exports. Outputs would be lower by 2% and exports by 5% in scenario 3. As farmed salmon is currently the UK's largest food export – the vast majority of which is farmed in Scotland – any reduction could have a significant and unfavourable impact on the industry and its future growth. Assuming other factors do not change, this may slow investment and growth in the

aquaculture industry, which to date has largely been driven by farmed salmon production, which would also have a potential detrimental impact to Scotland's economy.

Conclusions

Studies such as this one help develop our shared understanding of the potential risks and challenges arising from leaving the EU for key parts of Scotland's economy. It contributes to our growing evidence base and enables us to undertake a more rounded assessment of the impacts of EU exit.

The research shows that there are potentially benefits to our seafood industries from leaving the EU, that would arise from leaving the CFP and renegotiating higher quotas for shared fish stocks. But we know that achieving that in the short term is highly unlikely. And any such benefits seem likely to come at the expense of tariff free trade for some seafood businesses. Hence, this research confirms the Scottish Government's position on remaining in the European Single Market and a Customs Union with the EU, while being out of the CFP. This would be the best outcome for Scotland's seafood industries if the UK were to leave the EU, allowing us to minimise the impacts of tariffs and NTMs, while providing flexibility over the long-term to negotiate inward quota transfers through the existing annual coastal states process.

The research also shows that there is a balance to be struck between increasing TAC shares or fishing quota and getting tariff free trade with the EU. It also shows broadly, that the benefits of increased quotas to the seafood industries reduce with increasing tariff and NTMs. That clearly has a detrimental impact on key parts of those industries, including aquaculture and fish processing.

We should also not lose sight of other threats that EU exit poses to the Scottish seafood industries. Previous reports estimate that non-UK EEA workers account for 58% of the labour force in the seafood processing industry. Leaving the European Single Market, and losing freedom of movement, is expected to have significant negative impacts on the seafood processing industry and the wider supply chain.

The loss of non-UK EEA labour and its impact on competitiveness of the fish processing industry will lower the benefits of any potential increases in fish quotas. This is further specific evidence for the fishing industry to support the Scottish Government's policy, which we first set out in December 2016 that the UK should remain within the European Single Market and a Customs Union with the EU. Remaining in the European Single Market and a Customs Union with the EU does not only preserve the benefits of frictionless trade with the EU, it gives our industries continued access to non-UK EEA labour that would come with continued freedom of movement.

Moreover, the current EMFF programme, together with associated match funding, is set to provide £150 million in grant funding to Scotland's marine sectors and coastal communities over the period 2014 to 2020. While the research has not examined the impact of losing access to this funding, the Scottish Government would like to ensure support for all seafood industries to continue to realise their full growth potential.

The Scottish Government is currently considering how best to take forward the future management of Scotland's fisheries and seafood industries, if the UK leaves the EU. The findings from this scenario modelling suggest that the future prosperity of Scotland's seafood industries depends largely on the right exit scenario being negotiated by the UK Government. Given the findings of this research, it is clear that the Scottish Government's least worst outcome is also potentially the most beneficial for our seafood industries. But they also show that the wrong exit scenario could be potentially significantly harmful to those industries.



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