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**Research Report**

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## Deal or No Deal – What's at stake for ACP countries with a hard Brexit?

Bernhard Tröster

The recent political changes in the United Kingdom (UK) make a 'hard Brexit' increasingly likely. Such an outcome has important implications not only for the bilateral relations between the European Union (EU) and the UK but also for the 79 African, Caribbean and Pacific (ACP) countries which have close economic and political ties with both partners. As the future EU-UK relationship largely determines the UK's relations with third countries, the departure from the formal pathway of Brexit negotiations creates much uncertainty and reduces opportunities for ACP countries. Possible downside risks may, however, concern the area of development cooperation rather than in the much-discussed domain of trade policy.

### Implications of an orderly Brexit

After the Brexit referendum in 2016, the EU and the UK entered into negotiations to arrange for an orderly separation. At the initiative of the EU, the process was divided into two phases: The urgent and pending issues including citizen's rights, financial obligations and the Irish border should be agreed upon in a withdrawal agreement before future relations were to be negotiated in a second stage. The withdrawal agreement should ensure that Brexit happens in an orderly manner by the 31 October 2019 (initially by the 29 March 2019) and start a transition period that would last until the end of 2020 (which could be extended until 2022 if both parties agree). As EU law would still apply during the transition period, this model offered some breathing room to prepare new EU-UK institutional arrangements and time for administrations, businesses and citizens to adapt.

The Brexit deal negotiated between the EU and the UK government of Theresa May also considers issues that are highly relevant for ACP countries. Firstly, the UK is the second-largest aid donor among EU member states, and the third-largest contributor to the EU aid budget, accounting for about 15 percent. The exit deal fixes the UK's financial commitments to the EU budget until 2020 (or even until 2022 if extended), including the European Development Fund (EDF). Secondly, since the Cotonou Agreement as the framework for the EU-ACP cooperation will expire on February 2020 and the negotiations on a Post-Cotonou arrangement are impending, coordination with the UK concerning the contents of a future arrangement with the ACP countries would be facilitated by an orderly Brexit process. Thirdly, the UK remains a partner in all EU trade agreements until the end of the transition period. New trade deals between the UK and the ACP countries could be arranged in the meantime to avoid disruptions.

Thus, the formal pathway for the Brexit process would offer time for all partners to adapt to the new situation. At the same time, it reduced the risk of overlooking issues in rela-

tions with third parties. Without a Brexit deal, these coordination processes would become considerably more burdensome. For the majority of ACP countries, potential risks from a 'hard Brexit' will, however, emanate primarily come from potential shifts in development cooperation policies and not so much from sudden changes in trade flows.

### Impact of a hard Brexit trade chaos?

No other issue in the Brexit strategy of the current British government seems more clear-cut than the one about the prosperous future trade and investment relations with non-EU countries. The British Trade Secretary George Hollingbery expressed this view in front of ACP representatives in October 2018: "Brexit was not and never has been about the UK turning in to ourselves – it is about facing out to the world" (Hollingbery 2018). He promised that a trade boom would emerge, once the UK and ACP countries were free to strike new trade deals.

While it can take years to establish bilateral trade deals, the current trade regime between ACP countries and the UK would cease to apply abruptly in a 'No-Deal' scenario. At present, the main feature of the ACP-EU trade relations is the duty-free quota-free (DFQF) market access for ACP goods exports to the EU, including the UK. These preferences are carried on in the recently negotiated Economic Partnership Agreements (EPAs) between the EU and seven regional blocs of ACP countries, in which also ACP countries are committed to reduce tariffs and liberalise market access progressively. Thus, ACP countries would face tariffs on their exports to the UK once the UK cuts ties with the EU, causing potential disruptions to their outgoing trade flows. In the case of 'hard Brexit', these disruptions could become a reality as early as November 2019.

The British government has therefore taken measures to avoid disruptions in trade relations, in particular with ACP countries. A first safeguard is the 'Cross-Border Trade Act', which allows the UK to continue granting non-reciprocal

market access to developing countries equivalent to the EU's Generalised Scheme of Preferences (GSP) and Everything-But-Arms (EBA) system, and includes a 'least developed countries' (LDCs) services waiver. Thus LDCs would experience little changes under UK's EBA scheme, but the most important trade partners for the UK among the ACP countries, namely South Africa (33% of UK-ACP trade), Nigeria (15%), Kenya and Ghana (both 5%), would face tariffs on their exports to the UK in case of a 'hard Brexit'. As lower middle-income countries, Nigeria, Kenya and Ghana would fall into the GSP regulations with (reduced) tariffs on manufacturing goods. Exports from South Africa as well as Botswana and Namibia as upper middle-income countries would even be charged with MFN tariffs, which were already specified by the British government in March 2019.

The British government has therefore increased its efforts to sign post-Brexit deals as a second safeguard measure. These arrangements aim for a rollover of reciprocal preferences laid down in EU-trade agreements – under which the UK conducts 30% of its trade in goods with non-EU countries – in the event of a 'hard Brexit'. However, many FTA partners have reservations against the British initiative. Despite the increasing likelihood of a 'no deal', the UK has so far secured agreements with only a few FTA partners, covering only one-third of the UK's trade in goods under FTAs (which is equivalent to 10% of total UK non-EU trade flows in goods). Among them are three Economic Partnership agreements (CARIFORUM, Pacific, and Eastern and Southern Africa), but these include only 20 ACP countries.

The major UK trading partners among the ACP countries are not yet covered by post-Brexit deals, partly because some countries have no ratified trade deal with the EU. At the time of writing (August 2019), the regional EPAs of the West and East African regions (ECOWAS and EAC) are still in limbo and doubts remain whether all members will sign them.<sup>1</sup> Thus, most ACP countries have not yet established a trade arrangement with the UK for the post-Brexit phase. A closer look at the sectoral pattern of ACP exports to the UK reveals, however, why there is no urgent need to do so.

The vast majority of exports from middle-income countries are unlikely to be affected by UK tariffs in any Brexit scenario. These ACP countries continue to export mostly natural resources (oil, metals) and (unprocessed) agricultural goods (cocoa, coffee, fruits), which are already tariff-free under the GSP and the MFN regimes. Besides, the UK is not a major export destination for most ACP countries anymore. Only 4% of ACP exports went to the UK in 2017, compared to 10% in the early 2000s. The overall effects of a 'hard Brexit' on ACP exports might, therefore, be less severe, even though selected sectors such as the automobile sector in South Africa and the cut-flower business in Kenya and other UK-dependent supply chains might still be hit. On the import side, a 'no-deal' scenario would allow all ACP countries that have not signed a post-Brexit deal with the UK to avoid tariff reductions on UK products established under the EPAs. Again, the importance of the UK as a source of imports has declined in recent decades to 2% of total ACP imports.

Overall, the trade effects of a 'hard Brexit' are likely to be rather limited for most ACP countries either because of post-Brexit deals are already in place, or because of the composition of exports and the declining role of the UK in ACP trade in goods. This gives ACP policymakers some leeway for assessing potential new deals with the UK. However, the bright prospects for ACP countries, coming with new trade deals in a post-Brexit world as evoked some Brexiteers are far from certain.

### Going global with the UK?

Claims about prospering UK-ACP trade relations based on new trade deals tend to overlook two aspects, which determine the potential effects for ACP countries: Firstly, the binding restrictions imposed by WTO rules, secondly, the future EU-UK trade relations – which must be settled with or without an exit deal – and thirdly the current UK-ACP trade patterns.

At first sight, the freedom to strike new trade deals with the UK seems appealing for ACP countries, in particular for those with pending EPAs. However, the UK's ability to offer enhanced market access to third parties is strictly linked to the nature of its future trade relationship with the EU as the UK's most important trade partner. Strong adherence to the EU market and its regulatory framework reduces the policy space for the UK's external policies (the so-called 'Norway model'), or it almost excludes new trade deals entirely (in the case of a 'customs union'). To negotiate, on the other hand, FTA-like arrangements, i.e. deep and comprehensive trade agreements similar to e.g. the EU-Canada agreement CETA would imply a major rupture from the EU and bear substantial economic risks (see Bank of England 2018). Thus, Britain finds itself caught between a rock and a hard place. On the one hand, keeping close relations with the EU constrains its policy options for third-party deals. On the other hand, loosening links with the EU offer more policy space but imply substantial economic costs given the UK's close economic integration with the EU.

From the perspective of ACP countries, the UK's limited market access potential and the high economic uncertainties question the need for urgent trade deals with the UK. In addition, these arrangements need to be discussed in the context of other related issues. The UK could offer development-friendly agreements with more policy space compared to EPAs and financial assistance (see below). WTO rules on bilateral agreements would nevertheless require EPA-like reciprocal trade liberalization as soon as non-LDC countries are involved. Further, initiatives by the UK for enhanced co-operation with strategic partner countries or regions could undermine the coordination among ACP countries and recent initiatives for regional trade integration among African countries such as the African Continental Free Trade Area. The African Union might be the most suitable counterpart in negotiations with the UK, but it has not yet established itself as a partner in trade agreements and needs to align the manifold interests of the African countries in a common negotiating agenda.

Finally, the UK might urge ACP countries to engage in deals on services trade. Service sectors are not yet part of the EPAs, and the UK has a keen interest to promote its service industries, as it runs a growing trade surplus in services trade with almost all regions. Thus, there is a clear imbalance in case of reciprocal market opening. Again, the UK's negotiating position on market access offers in services sectors is highly dependent on the future EU-UK trade arrangements, given the close integration of e.g. financial services industries with the single market. Further, negotiations on services trade liberalization are typically complex and related to sensitive issues, such as investment or public procurement.

All in all, the prospects for new trade deals to 'go global' with the UK are possibly less bright than promised. ACP countries should carefully weigh their interests before rushing into new trade arrangements. An orderly Brexit would provide such breathing room for negotiators.

### **Charting unknown terrain in development cooperation**

The development policy of the EU constitutes an area with shared competence between EU institutions and member states. The coexistence of a European as well as 28 national development cooperation policies always has required coordination. In case of the Brexit, the continuation of such coordinative actions could be facilitated by the withdrawal agreement, in particular as it ensures UK's financial contributions to EU development instruments. As the second-largest aid donor in the EU, the UK contributes 1.5 million GBP to EU ODA, of which two-thirds go to the official EU budget and one third to the EDF. The UK's rolling commitments in the Brexit deal for EU development cooperation facilities are estimated at GBP 4 billion (Edwards 2018). In the case of a 'hard Brexit', it is uncertain whether this volume of ODA will be preserved and for which focal regions and topics it will be used.

While ODA has not been prominent in Brexit campaigns, some Brexiteers have already called the role and purposes of development aid after Brexit into question. Thus, a reduction of the UK's ODA level cannot be ruled out, particularly, if Brexit generates adverse effects on the UK's economic prospects. But even with a continuation of ODA volumes, a re-direction of British ODA funds towards strategic partner countries and uses that serve the UK's geopolitical and economic interests is most likely. This will also include stimulating trade and private sector-led development and a possible bundling of aid and trade (Lightfoot et al. 2017). Such arrangements, it is needless to say, might not necessarily be beneficial for most ACP countries (as discussed above).

A disentangling of the UK development policy from the EU and a shift in the UK's aid strategy would affect the EU development cooperation agenda. So far, the UK has promoted results orientation in EU development policies as well as gender issues and good governance. It remains unclear which other EU member states should push these agendas forward in the future. Moreover, it is difficult

to compensate for the UK's close political links with particular regions and countries. Thus, the global ambition of EU development policy would suffer because of lower financial resources and reduced political influence after Brexit. Consequently, debates on the strategic aims of development cooperation and the design of EU aid facilities have intensified among the remaining EU member states in the context of the upcoming EU budgetary framework (MFF 2020-2027) and the political agenda of the new European Commission under President Ursula von der Leyen.

The consequences of these changes for ACP countries are apparent in the negotiations on a successor agreement to the Cotonou Agreement, which expires on February 2020. Since the Lomé Convention, which had been concluded after Britain's accession to the European Community in the 1970s, the comprehensive EU-ACP agreements have been regarded as a core element of the common European development policy. Shifts in regional priorities of the UK and the EU as well as dynamics within and between the ACP regions, however, question the continued relevance of this institutional framework.

The EU's negotiating mandate for the Post-Cotonou Agreement seems to offer a possible solution. The future EU-ACP agreement should consist of a superordinate part and three specific agreements with the Caribbean, Pacific and African regions. This corresponds to the desire of African countries for closer cooperation with the EU as well as to the ACP Group Secretariat's claim for legal representation. Nevertheless, the remaining EU-27 must re-adjust the relationships with Caribbean and Pacific countries, which have strong historical ties to the UK. Within the EU-Africa relations, there are warnings of a future imbalance between French-dominated West Africa and the countries of Eastern and Southern Africa. If the EU places more emphasis on security and migration in the ACP agreements, as demanded by Eastern European states, this will strengthen the regional focus on West and North Africa. Recent initiatives such as the Compact with Africa of the G-20 and the Marshall Plan with Africa (both on Germany's initiative) are already focusing primarily on those countries.

Even though the EU is planning to include 'like-minded' countries to the Post-Cotonou agreement, a 'hard Brexit' would complicate the coordination of development agendas between the EU and the UK significantly.

### **Going for a triangular relation**

The separation of the UK from the EU creates uncertainty for ACP countries, in particular in the case of a 'hard Brexit'. These risks are not so much related to trade effects, as most ACP countries will experience little changes in their market access after Brexit, but are linked to a possible change in development cooperation. Here, the UK and the EU might shift the strategic orientations of their development agendas simultaneously without much coordination, with adverse effects for certain 'non-strategic' ACP countries or regions.

As the future links with ACP countries depend directly on the future EU-UK relationship, ACP countries should have a vital interest in an orderly Brexit process as foreseen by the withdrawal agreement. During the transition period, ACP countries could bring their concerns to the official negotiation tables. Moreover, ACP countries would have the possibility to explore their priorities for future trade negotiations. Similarly, with respect to development cooperation, institutional mechanisms for the coordination of strategic priorities between the EU, the UK and the ACP countries could be built up. Under a 'hard Brexit' scenario, the risk is, however, significant that the strategic trajectories of development cooperation policies of the EU and the UK will follow diverging routes. This may limit ACP countries' development perspectives, especially for 'non-strategic' countries and regions.

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- 1 The seven EPA blocs do include all ACP countries, but not all ACP countries have entered into the EPA negotiations and agreements. For instance Ethiopia in the Eastern and Southern Africa (ESA) EPA or Angola in the Southern African Development Community (SADC) EPA. (see also <http://ec.europa.eu/trade/policy/countries-and-regions/development/economic-partnerships/>)



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