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In two decades, EU Customs Union membership has not delivered clear benefits for any major UK sector



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There's a difference between what the Customs Union was supposed to achieve in theory and what it's actually achieved in practice. Thanks to historical trade data published by the UK Office for National Statistics (ONS) in September 2018, we now know the difference is huge. By making multiple comparisons in UK, EU and non-EU trade since 1998, it's possible to judge the UK's record inside the Customs Union over the past 20 years, and assess the value of seamless, tariff-free trade with the EU in terms of what it's actually achieved.

All my data is sourced from ONS September 2018 release unless otherwise stated and compiled in two spreadsheets: UK's Top Ten Sectors (http://2mbg6f gb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UKs-Top-10-sectors_BC.xlsx), which analyses each principal UK traded sector in turn, from motor vehicles to beverages; and UK Trade in Goods & Services (http://2mbg6f gb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UK-Trade_Goods-and-Services_BC.xlsx) which directly compares UK's trade in goods and services. Both cover the period 1998 to 2017 and I would encourage readers to download and inspect them.

EXPORT GROWTH: 1998 TO 2017

For a first-pass assessment of UK's traderecord in the Customs Union, divide all UK exports into four, roughly equal parts: exports of goods to the EU (worth £164 billion in 2017); exports of services to the EU (£117 billion); exports of goods to non-EU countries (£175 billion); and exports of services to non-EU countries (£162 billion). Now, using the historical trade data published by the ONS in September 2018, calculate the average yearly growth rate for each of these four categories from 1998 (or 1999 for the services data) to 2017 (the method used is to take a three-year average at the start and end of the time period, and then adjust for inflation using the ONS' own import/export deflator).

The results are perverse. The UK's slowest-growing export trade since 1998 is goods exports to the EU, which have grown by just 0.2% per year since 1998, or 3.7% over 20 years. Yet this is precisely the sector that is supposed to benefit from tariff-free trade within the Customs Union. And even 0.2% is misleading. Most growth occurred pre-2007; adjusting for inflation, average annual exports in 2008–2017 were actually lower than 1998–2007 (See Tab 3 in UK Trade in Goods & Services (http://2mbg6fgb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UK-Trade_Goods-and-Services_BC.xlsx), Section 2, line 77. £144.7 bn as opposed to £145.6 bn in 2015 prices).

Conversely, the UK's fastest growing exports are services exports outside the EU, unimpacted by either the Customs Union or Single Market regulation. At 5.6% per year over 20 years, these exports have grown so fast in the last 20 years, they are now worth almost as much as UK's entire goods exports inside the Customs Union.

Next fastest is UK's services exports to the EU, growing an impressive 5.2% per year. This sector is marginally impacted by the Single Market. A portion of financial services are impacted by EU regulation, although financial services exports contribute just under one-third, or 31% of UK services exports to EU. (Overall, just 11% of UK services exports are financial services exports to the EU – for a breakdown of UK's services trade see Tab 2, UK Trade in Goods & Services (http://2mbg6fgb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UK-Trade_Goods-and-Services_BC.xlsx)).

Meanwhile UK's goods exports to countries outside the EU countries – and outside the Customs Union – have grown at a crisp 3.3% per year since 1998. This sector is heavily influenced by the Single Market, whose rules apply to most goods made in UK, but they are conducted outside the Customs Union. And thanks to the trade-database research of Michael Burrage, *It's Quite OK to Walk Away*

(<https://www.civitas.org.uk/content/files/itsquiteoktowalkaway.pdf>), we can approximately calculate the proportion of UK's non-EU exports that has been conducted on World Trade Organisation (WTO) terms.

Taking the year 2015, Burrage estimates that 6% of UK's exports went countries with whom UK enjoys an EU-negotiated free trade agreement (FTA). Another 8% went to European Free Trade Agreement markets. This means, approximately 73% of UK's exports to non-EU countries was conducted on WTO terms. Much of the rest (principally Switzerland) is with countries that impose near-negligible tariffs on non-food imports.

Consequently, the 3.3% per year growth rate achieved by UK's non-EU goods exports is a strong and accurate reflection of UK companies' ability to trade on WTO terms. Since 1998, UK businesses have proved more adept at growing markets outside the Customs Union than in it, despite the tariff and customs barriers they confront in most non-EU trade. Meanwhile, UK businesses have failed to grow markets inside the Customs Union, despite the fact that this trade with the EU is tariff free.

What's to blame for this discrepancy – or more accurately, what's not to blame – will be analysed in Part 3 of this analysis, when UK's export growth is compared to Euro-area growth, intra-EU trade, UK productivity, and EU–US trade over the same period. But in a straightforward assessment of the value of the Customs Union to UK, the data are unforgiving: that part of UK exports that is governed by the Customs Union is easily UK's worst performing.

THE CUSTOMS UNION: QUI BONO?

Not so with EU imports, however. Back in 1998, UK's EU goods trade was roughly in balance, (-£5.6 bn in current prices). But since then, imports from the EU have grown at a strapping 3.4% per year. The import sectors displaying the fastest growth are motor vehicles, (with imports growing 3.6% p.a., to reach £47.7 bn in 2017), food products (5.3% p.a., to £23.2 bn) and pharmaceuticals (7.3%p.a., to £22 bn), with this last import category showing especially rapid growth since 2011.

So, since 1998, the track record of the Customs Union has been to take a trade relationship that was trim and balanced and turn it into a £95 billion deficit, which is larger – per head – than the US trade deficit with China.

Here again, the ONS November-release trade data helps because we can see to what extent UK's services trade with the EU will ever balance this equation out. And the answer is: it won't.

Services exports to EU may be growing nicely (5.2% p.a., as opposed to services imports growth of 3.0% p.a.) but the £36 bn surplus it generates pays for just one-third of UK's deficit in trade in goods. And since the difference between UK's goods export-import growth rate (3%) is wider than the difference in the UK's services export-import growth rate (2.2%) it never will – so long as UK maintains its current terms of trade with the EU.

The perverseness of UK's EU-trade outcomes extends to the deficits UK incurs on those individual trade sectors most impacted by the Customs Union (See Tabs 2-11 of UK's Top Ten Sectors (http://2mbg6fgb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UKs-Top-10-sectors_BC.xlsx). Data for each sector is presented in turn, in order of the total value of UK exports. Together, these top ten sectors contribute 80.9% of UK manufacturing exports, or 71.1% of UK goods exports). The UK's two biggest two-way trade sectors with EU are motor vehicles (worth a combined £67.3 in 2017) and food & agriculture (£39.8 bn). These are also the two sectors where the EU's common external tariff (CET) exerts the biggest impact on UK trade, and theoretically provides the greatest 'protection'. Yet these are simultaneously the sectors where UK incurs its biggest deficits (See Tab 1, UK's Top Ten Sectors (http://2mbg6fgb1kl38ogtk22pbxgw-wpengine.netdna-ssl.com/wp-content/uploads/2019/02/UKs-Top-10-sectors_BC.xlsx). 'Manufacturing').

Both of these deficits have increased dramatically since 1998: by £19.2 bn (current prices) for motor vehicles, and £14.1 bn for food & agriculture. These deficits reflect a surge in imports from fellow Customs Union member states, for which no commensurate reciprocal gain or trade-off can be found in any other sector of UK's goods trade. In other words, there is no trade-off within the Customs Union.

At this point in the analysis, it's worth stepping through the 20-year trajectories of each of UK's top ten goods-trade sectors to try to map supposed tariff-free advantage with actual outcome. What you find is either a sizeable and growing deficit: food products (-£14.4bn); and beverages (-£2bn); or stagnant growth plus a sizeable deficit: motor vehicles (0.4% p.a., -£28.bn); machinery (-0.1% p.a., -£7.2bn); chemicals (0.7% p.a., -£3.5 bn); computers and electronics (-5.8% p.a., -£11.3 bn); basic metals (1.% p.a., -£3.4 bn); and electrical goods (-0.9% p.a., -£4.4 bn). Since we have now compassed 72% of UK's goods exports, the obvious verdict is hard to swerve.

Damningly, the only two of UK's top-ten EU traded sectors that have performed strongly since 1998 derive next-to-zero commercial advantage from the Customs Union. The UK's second biggest export sector – transport equipment, which is 92% aerospace related (and therefore trades tariff-free) – has climbed a decent 2.7% per year. And UK's pharmaceuticals exports (up 6.3% p.a. to EU, since 1998) gain minimal competitive advantage because major developed economies abolished tariffs on end-user pharmaceuticals during the Uruguay Round, which concluded in 1993.

So, on the basis of the UK's own 20-year trade data, *there is not one, single major sector of trade* in which the Customs Union has delivered clear, demonstrable benefit to UK since 1998. Shown in aggregate, across all UK trade, the failure is stark. What's troubling – for UK consumers, at least – is that the Customs Union appears to be turning the UK into a series of tightly controlled captive markets for EU producers. To see how, I shall in due course take a detailed look at the 20-year history of UK's two biggest EU traded sectors – motor vehicles and food.

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