Cebr

irwinmitchell
private wealth

The Impacts of Brexit on the Rural Economy

April 2019

Welcome

Welcome to the **latest economic report** from Irwin Mitchell, which examines the impact of Brexit.

Although the rural economy has a huge role to play in the UK, it is often overlooked in much of the current economic analysis.

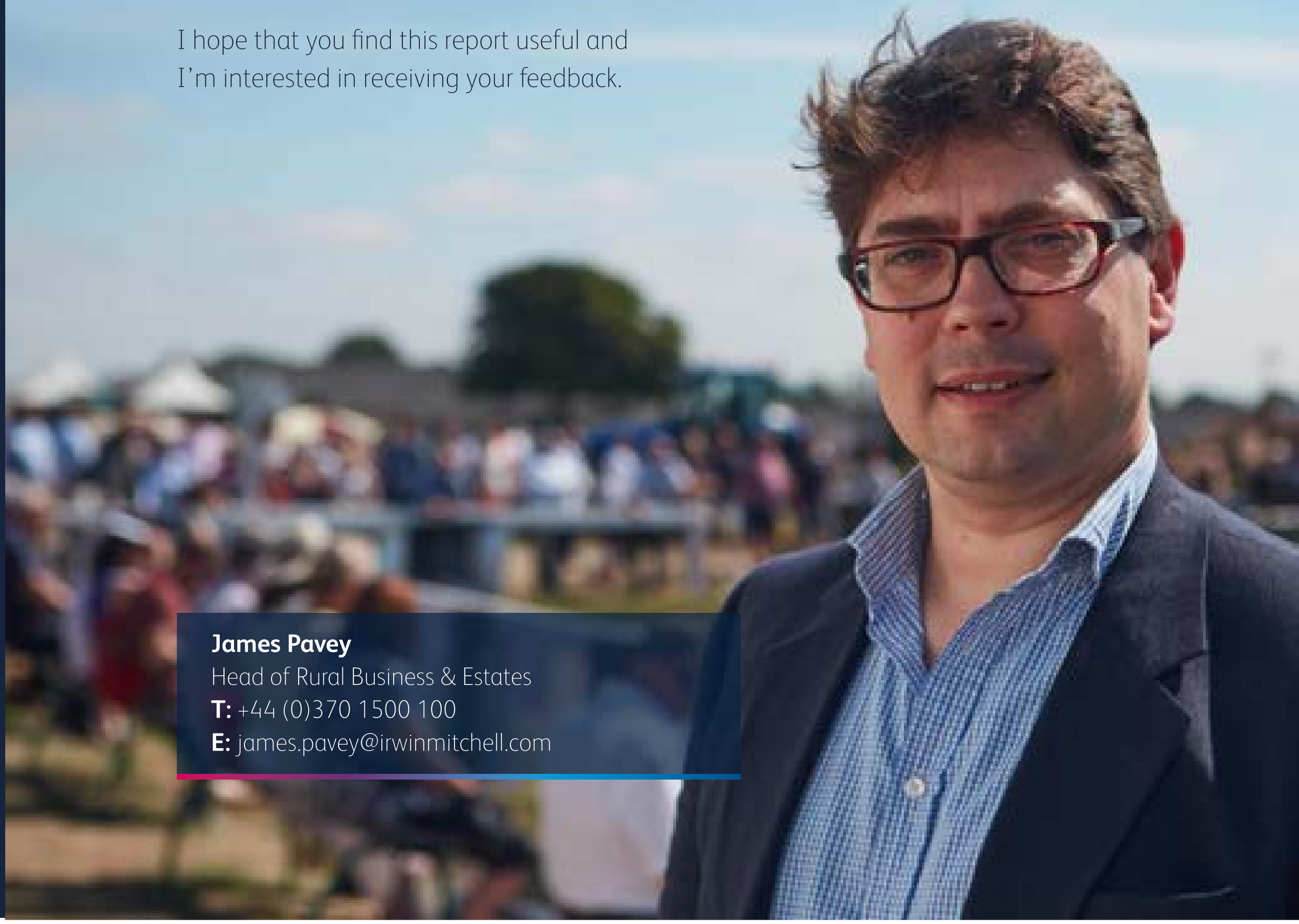
Many would expect the rural economy to experience slower growth when compared with the urban economy, with a narrower range of sectors and a focus on farming and other agricultural work.

This latest report, which has been produced by the Centre for Economics & Business Research (Cebr), highlights that this isn't the case.

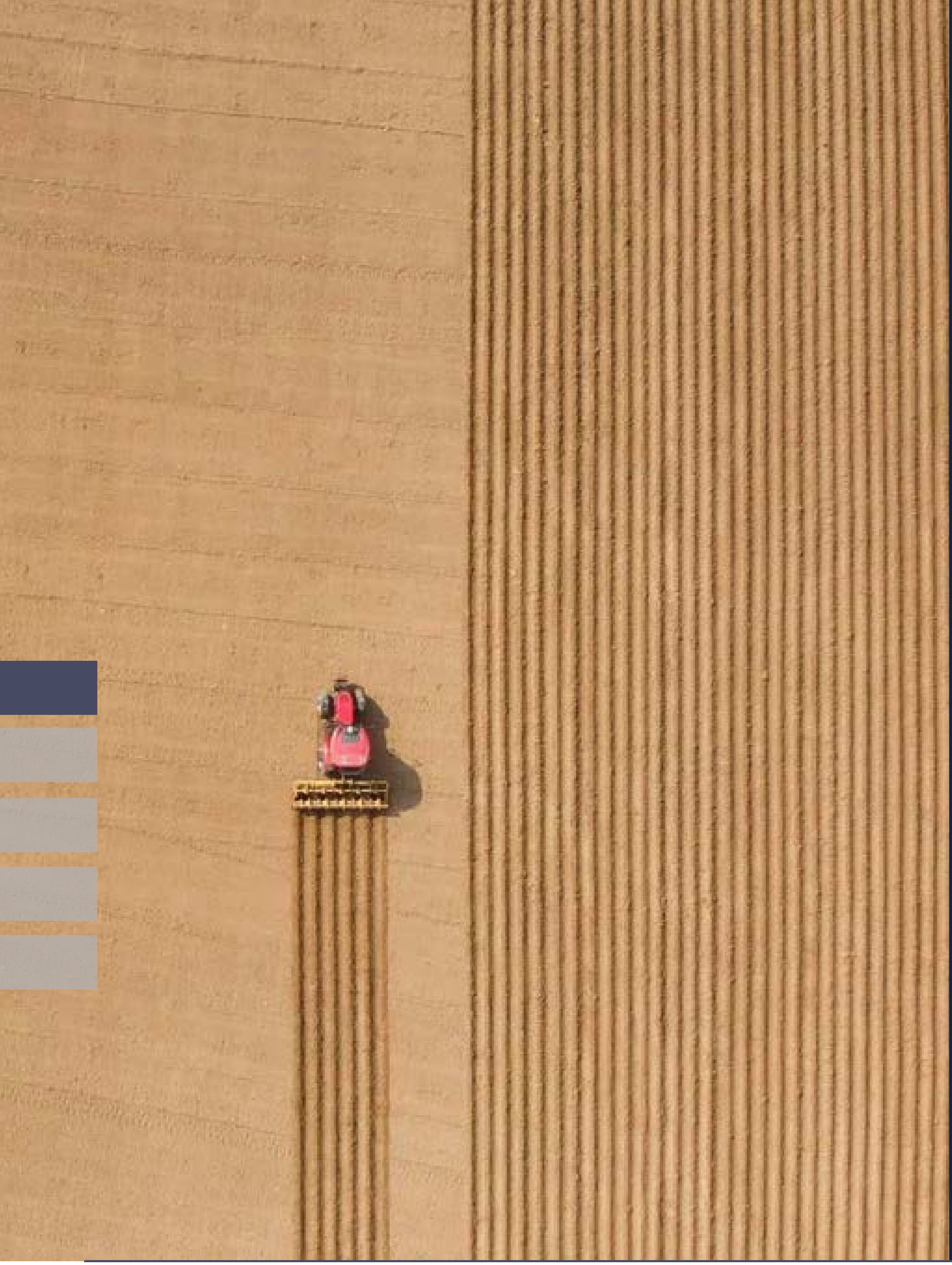
The study, in fact, highlights that in 2019 and beyond, gross value added (GVA) in rural areas will actually grow more quickly than in UK towns and cities. It also reveals that while urban areas have a higher number of workers in every industry, most industries actually make up a similar share of the economy in rural and urban areas.

Despite this growth, the rural economy certainly faces a number of challenges as a result of Brexit in terms of the supply of labour, tariffs and competition from other countries. This report examines these, as well as also looking at the opportunities that are presented by diversification.

I hope that you find this report useful and I'm interested in receiving your feedback.



James Pavey
Head of Rural Business & Estates
T: +44 (0)370 1500 100
E: james.pavey@irwinmitchell.com



Key findings

Most industries make up a similar share of the economy in both rural and urban areas, highlighting similarity in their 'make-up.'

Employment and GVA growth are set to differ between urban and rural areas. In 2019, urban areas are expected to see GVA growth of 1.2 %, while rural areas and mostly urban with some rural areas are both set to see growth rates of 1.6 %. By 2023, it's forecast that urban growth will increase to 1.6 %, while rural and mostly urban with some rural areas will see growth of 1.7 %.

Urban areas and mostly urban areas are expected to see a 1 % increase in the number of people in work. Rural areas are forecast to see growth of 0.8 %.

Brexit stands to affect a significant share of trade in the agricultural sector. EU countries were the destination for 60 % of UK food, feed and drink exports in 2016, whilst the UK was dependent on EU member states for 70 % of its imports in these areas.

The UK's agricultural sector relied on 27,000 workers from other EU member states in 2016. Estimates suggest EU labourers make up 98 % of the extra 75,000 seasonal workers needed each year. These workers stand to be impacted by the end of free movement of labour in a no-deal Brexit.

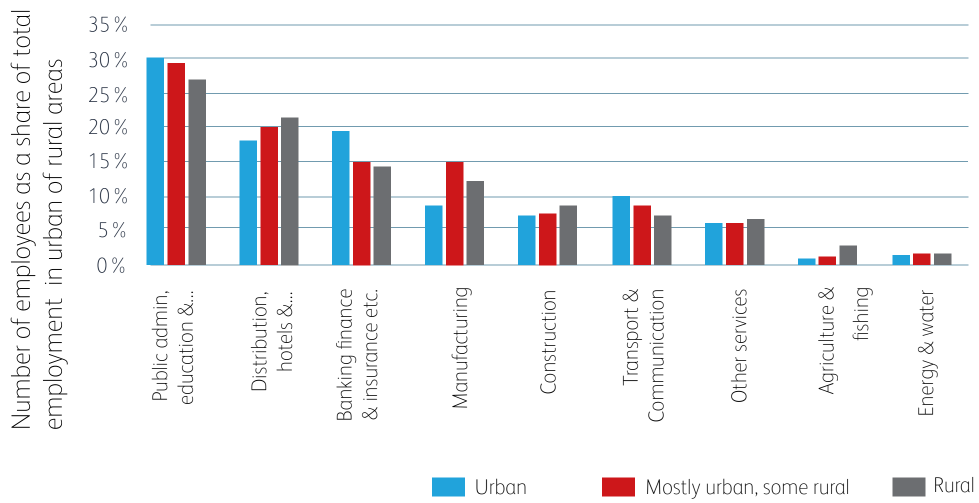
According to Department for Environment Food and Rural Affairs (Defra), more than half of England's 57,000 farms diversified in some form in 2016. Total income from diversification activities was £580 million in 2015/16, up 9 % from the year before and made up 32 % of total farm business income.

Businesses in the agricultural sector have real and current opportunities for diversification into a number of activities – tourism, environmental protection and horticulture.

Taking stock of the rural economy

Urban areas have a higher number of workers in each industry, but, as a percentage of total employment, industries make up a similar share in both rural and urban areas. This highlights that there's more similarity in their 'make-up' than might otherwise be assumed.

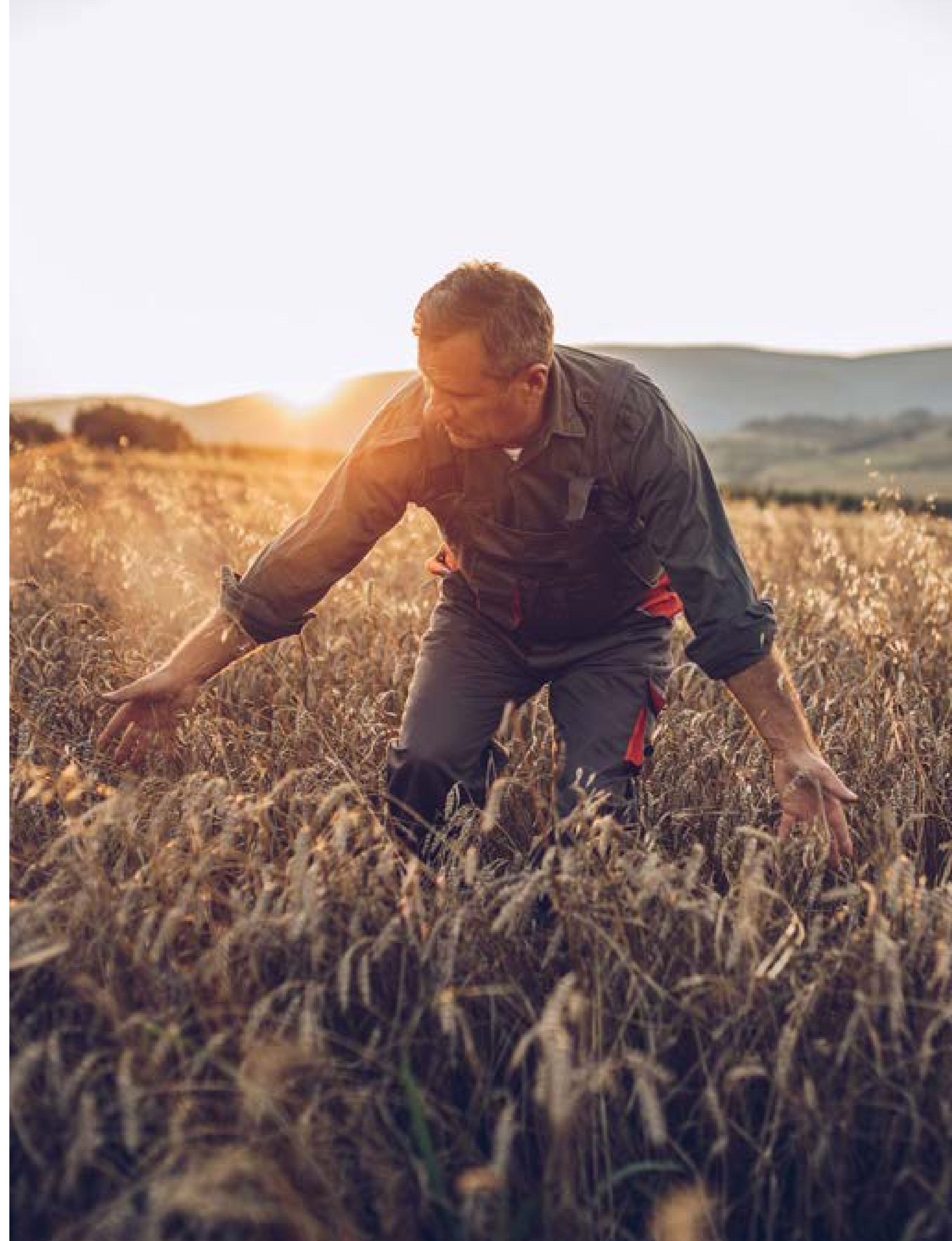
Figure 1 - Employment by industry and urban/rural areas in England, 2017[1]



Source: Nomis, Cebr analysis change 'mostly urban…' to 'Mostly urban with some rural' in key

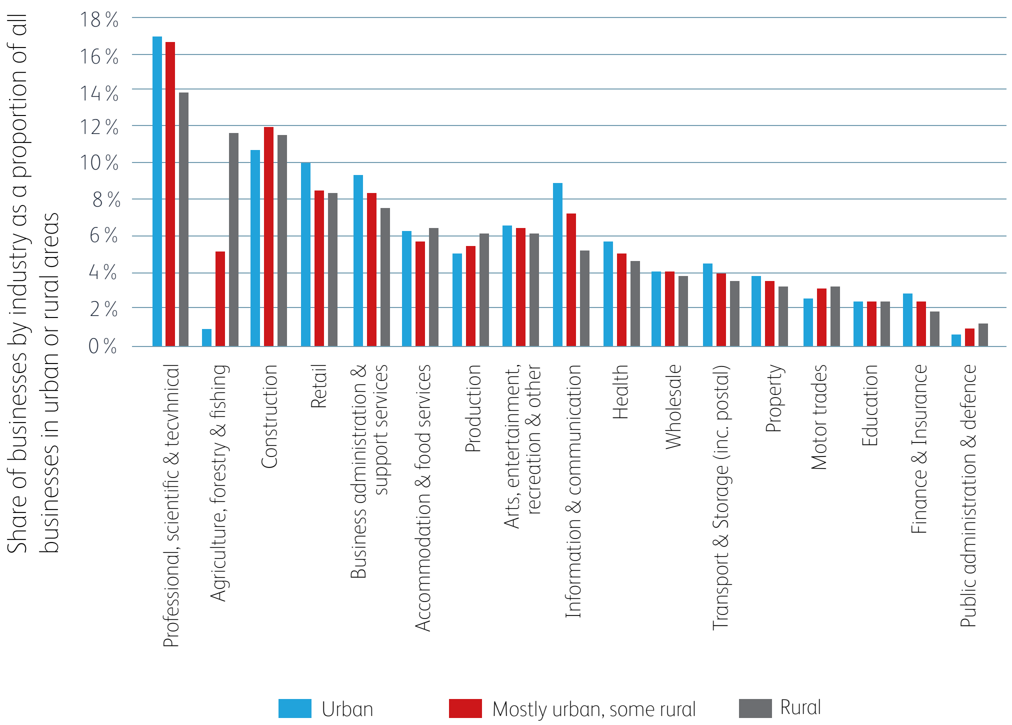
The biggest employer in all areas is the public sector. In 2017, approximately 1.2 million people were employed in public administration, education and health in England's rural areas, accounting for 27 % of workers.

1 'Urban' refers to the predominantly urban ONS definition, 'mostly urban with some rural' refers to the urban with significant rural ONS definition, 'rural' refers to predominantly rural ONS definition.



After the public sector, the industry with the next highest employment in rural areas was the distribution, hotels and restaurants sector with 21 % of workers. This share is higher than in urban (18 %) and mostly urban areas (20 %).

Figure 2 - Share of businesses in urban/rural areas by industry in England

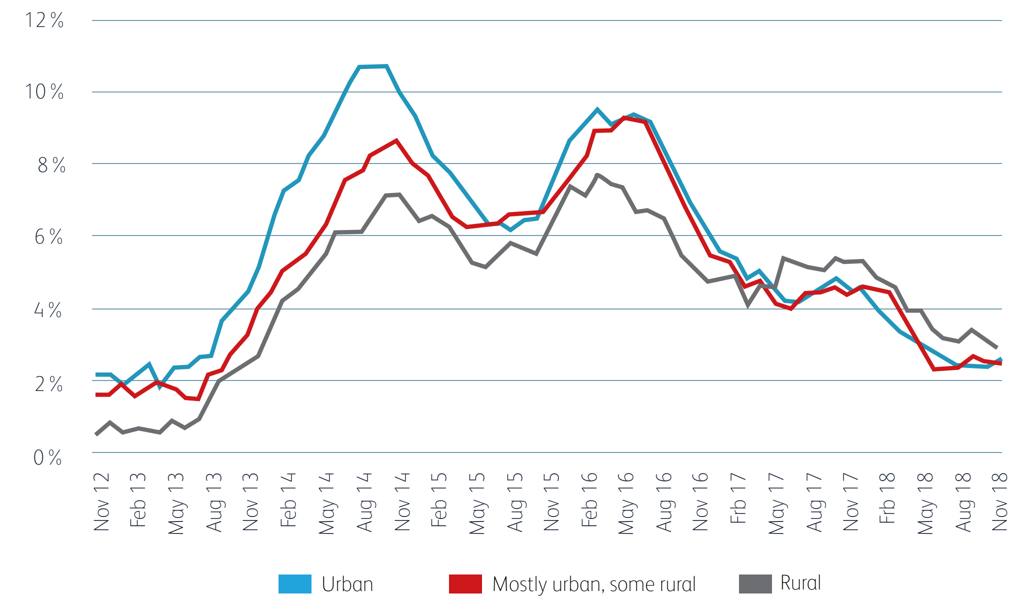


Source: ONS, Cebr analysis

In the majority of cases, there's no more than a 2 % difference between the share of businesses that industries make up in rural and urban areas. For instance, the property sector makes up 4 % of businesses in urban areas and 3 % in rural areas.

There are just three instances when this is not the case: information and communication; professional, scientific and technical; and agriculture, forestry and fishing. The latter has the largest discrepancy between rural and urban areas, making up just 1 % of businesses in urban areas but 12 % in rural areas.

Figure 3 - Annual growth in house price index, by urban/rural in England



Source: Land registry, Cebr analysis

The rate of change in house prices for all areas accelerated between November 2012 and November 2014, with the steepest rises in urban areas. But since mid-2016, shortly after the UK voted to leave the EU, house price growth has shown a downward trend.

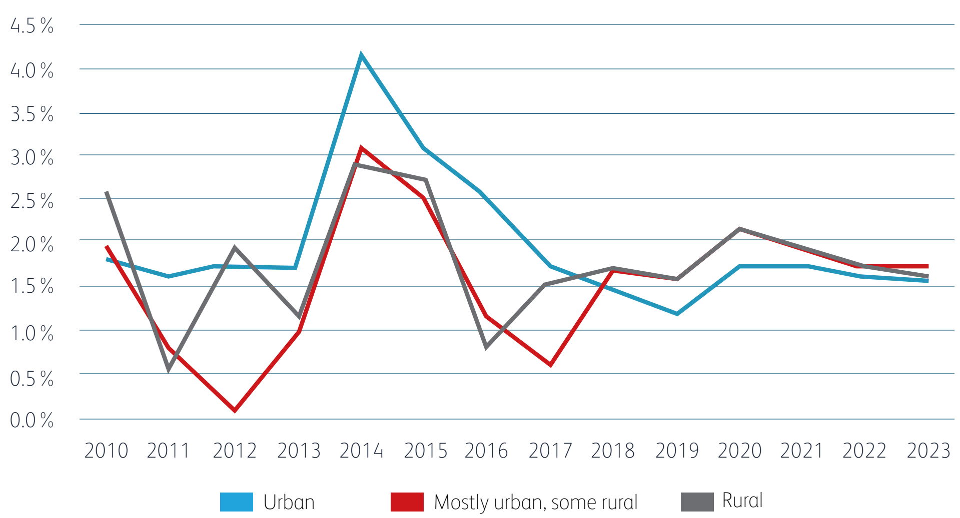
Although house prices have moved in tandem over time, from November 2012 to March 2017 rural house price increases were consistently below those in urban and mostly urban areas. This trend was reversed in Q2 2017, although by November 2018 there was convergence in the rate of house price changes across all areas. The slower rate of price growth across both rural and urban areas is indicative of the current weakening of the UK housing market, where activity remains subdued. In 2018, house prices suffered a bigger post-summer dip than usual as Brexit negotiations intensified, falling from a peak of £232,797 in August to £230,630 in November.

The situation is unlikely to improve following Brexit, and the severity of the impact will depend on whether or not the UK leaves the EU with a deal. In September 2018, Bank of England governor Mark Carney warned that leaving the EU without a deal could send house prices tumbling by a third.[2] This will be felt across both urban and rural areas, and will most likely subdue price growth further in the months ahead.

2 BBC News. https://www.bbc.co.uk/news/business-45516678

A look ahead

Figure 4 - Annual gross value added (GVA) growth forecast by urban/rural in England



Source: ONS, Cebr forecasts

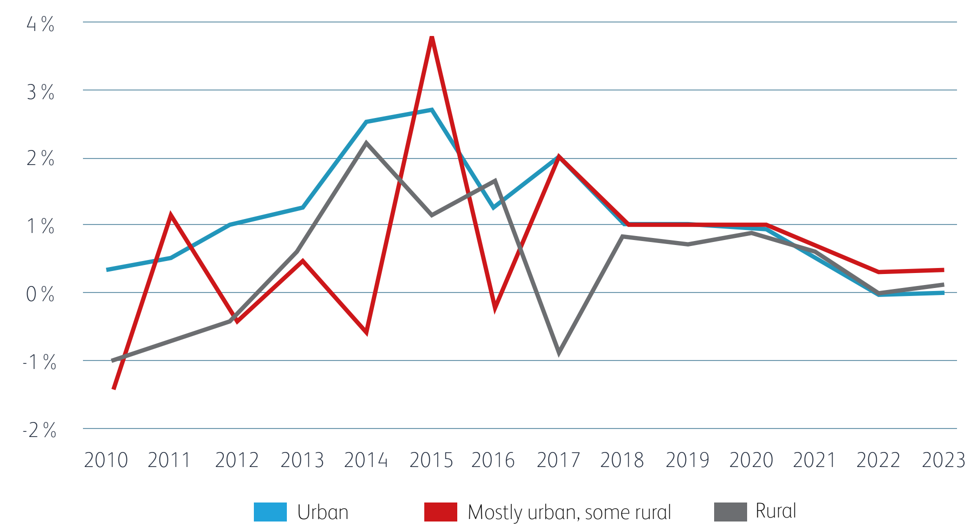
Historically GVA growth in urban areas has been faster than in more rural areas.

Since 2010, GVA growth in all three regional types – 'urban,' 'mostly urban with some rural' and 'rural' – peaked in 2014, when we saw annual growth rates of 4.1 %, 3.1 % and 2.9 % respectively. Between 2014 and the latest official data (2017), growth has slowed across both urban and rural areas, but the deceleration has been greatest in urban areas.

Looking towards 2023, urban areas are expected to see a slower growth rate than the other regional types. In 2019, urban areas are expected to see growth of 1.2 %, while urban with some rural and rural areas are both set to see growth rates of 1.6 %. By 2023, Cebr forecast that urban growth will increase to 1.6 % annually, while rural and urban with some rural areas will see growth of 1.7 %.

The relatively high growth forecast for rural regions compared to urban regions is, in part, driven by the high growth forecast for local authorities in the East of England and the Midlands. The life sciences and advanced manufacturing industries in these comparatively less urban regions are expected to be a significant driving force of GVA growth in the coming years.

Figure 5 - Annual employment growth forecast by urban/rural in England



Source: ONS, Cebr analysis

Turning to employment growth, urban areas are expected to see faster growth than more rural areas in the period to 2023. In 2019, urban areas and urban with some rural areas are expected to see the number of people in work grow by 1 %. Meanwhile, rural areas are forecasted to see annual growth of 0.8 %. By 2023, employment growth is set to slow to 0.4 % in urban areas and 0.1 % in rural areas.

Urban areas have a higher number of workers in each industry, but, as a percentage of total employment, industries make up a similar share in both rural and urban areas. This highlights that there's more similarity in their 'make-up' than might otherwise be assumed.

The biggest employer in all areas is the public sector. In 2017, approximately 1.2 million people were employed in public administration, education and health in England's rural areas, accounting for 27 % of workers in rural areas. After the public sector, the industry with the next highest employment in rural areas was the distribution, hotels and restaurants sector with 21 % of workers. This share is higher than in urban (18 %) and mostly urban areas (20 %).

Brexit and agriculture

According to Defra[3], EU countries were the destination for 60 % of UK food, feed and drink exports in 2016. Similarly, the UK was dependent on EU member states for 70 % of its imports in these areas, accounting for 30 % of total UK food consumption. This illustrates the significant share of trade in the agricultural sector that stands to be affected by Brexit.

The government's publication of its proposed temporary tariff schedule shows that, in the case of a no-deal Brexit, 87 % of total imports to the UK by value would be eligible for tariff-free access. However, tariffs would still apply to 13 % of goods imported into the UK. In order to support farmers and producers who have historically been protected through high EU tariffs, this would include a mixture of foodstuffs, such as lamb, pork, poultry and some dairy.

3 Department for Environment Food & Rural Affairs. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/672119/AUK-2016-08jan18.pdf

Despite these attempts to protect UK farmers, all exports from the UK will face barriers to entry in other countries in the form of higher tariffs, unless otherwise negotiated in bilateral trading agreements.

As well as tariffs, agricultural products set for export from the UK will be subject to other checks before entry into EU member states. While it's unclear how long these checks will take at various borders, it does place pressure on an organisation's inventory and stock levels, which may be unpredictable as the UK adjusts.

As UK producers come into direct competition with farmers worldwide, it will shine a light on their relative inefficiency – a significant threat for the agricultural sector.

For instance, South American beef producers are currently priced out of the EU market by tariffs. Should the UK leave the EU without a deal, it would open up a tariff-free quota of 230,000 tonnes to all countries with a licence to export to the UK. This quota, manged on a first-come-first-served basis, would place Irish beef farmers – responsible for providing the bulk of UK beef imports – in direct competition with their counterparts in Brazil and Argentina. According to the Agriculture and Horticulture Development Board (AHDB), South American countries have significantly lower costs of production than the UK and this will give them an advantage, whilst placing UK farmers under significant pressure.[4]

Should the UK leave the EU without a deal, it would open up a tariff-free quota of 230,000 tonnes to all countries with a licence to export to the UK.

The UK's agricultural sector currently relies heavily on EU nationals for labour, and faces a substantial challenge to its supply post-Brexit.

In a study completed by Northern Ireland's Department of Agriculture, Environment and Rural Affairs, 35 % of farms surveyed used migrant labour from the EU in November 2017. Of these respondents, 97 % indicated that this migrant labour was important and very important in 66 % of cases. When asked about the impact of Brexit, 34 % of these farm owners claimed they would reduce production, decreasing output from the Northern Irish farming industry. These concerns are likely to be mirrored across the whole of the UK, where 27,000 people from other EU member states worked in UK agriculture in 2016.[5]

4 https://www.fginsight.com/news/news/south-american-beef-farmers-poised-to-benefit-from-no-deal-brexit-tariffs-82445

5 https://researchbriefings.parliament.uk/ResearchBriefing/Summary/CBP-7987#fullreport

Seasonal migrant labourers are especially vulnerable. Estimates put EU labourers at 98 % of the 75,000 seasonal workers needed each year, all of whom stand to be impacted by the end of free movement in a no-deal. A nationwide pilot to bring migrant workers to UK farms was announced by the Home Secretary and Environment Secretary in September 2018. The pilot will mean fruit and vegetable farmers are able to employ migrant workers for seasonal work for up to six months. Under the two-year scheme, 2,500 workers from outside the EU will be able to come to the UK each year. This will alleviate some, but not all, of the labour shortages during peak production periods.

While much of UK trade after Brexit will fall under World Trade Organisation (WTO) rules, in the event of a no-deal Brexit there remains scope for the UK to develop its own legislation, detailing checks for its imported agricultural goods. This legislation will need to provide a framework for the environmental and safety standards of food coming into the UK. It will directly cover the safety and quality of food, feed, plant health, animal health and welfare in the agricultural sector. New policies will aim to keep the UK competitive on the world stage, as it seeks to remain attractive to its trade partners.

Other scenarios besides a no-deal are still available to the UK, and an agreement that maintains similar trade arrangements to those that currently exist, or a deal with a looser agreement between the UK and EU, could be negotiated.

In the former case, the UK agricultural sector would benefit from the greater certainty that would arise from the continuity of current trading agreements. A close post-Brexit relationship with the EU would, most probably, restrict the UK's ability to implement its own legislation determining trade agreements with countries outside of the EU.

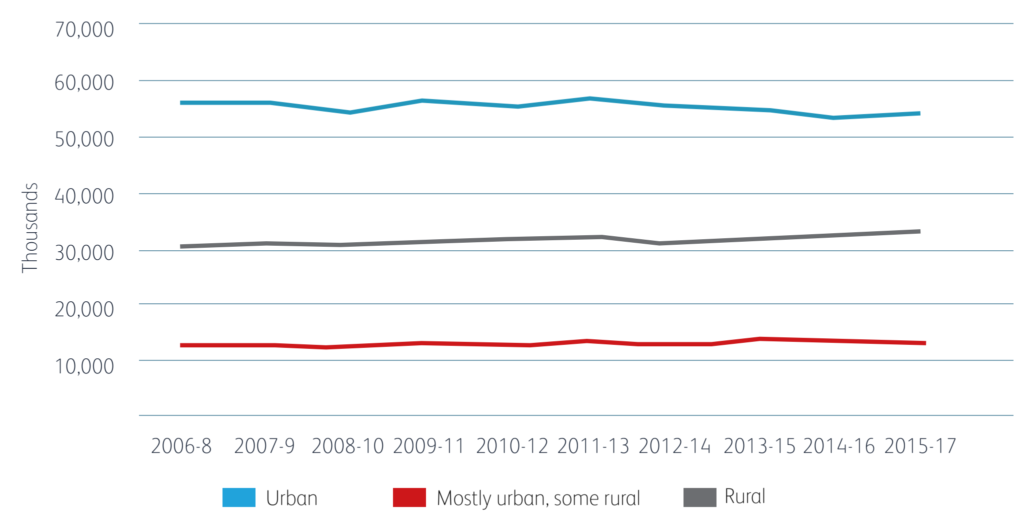
Instead, under such an agreement, the UK would likely be required to comply with EU standards, as well as a high number of EU rules and regulations. This type of agreement would probably require the UK to maintain freedom of movement. However, this is a compromise that the UK government has insisted it won't make, rendering this type of outcome unlikely without a significant change of approach.

Diversification

British farms receive approximately £3 billion a year from the EU[6] as part of the Common Agricultural Policy (CAP). The prospect of losing some or all of this income, as well as trade embargoes on their products, will severely impact production and revenue in agriculture.

If the UK departs from the EU without a deal, exports of animals, animal products and produce from the UK may stop temporarily. Should a deal be agreed before the deadline, which allows some reduced level of tariffs to the EU, the UK will still face barriers on its agricultural output from third parties. This should make diversification a high priority for agricultural businesses. In fact, more than half of England's 57,000 farms diversified in some form in 2016 according to Defra. The total income from diversification activities was £580m in 2015/16, up 9 % from the year before, and making up 32 % of total farm business income.[7]

Figure 6 - Total trips to the UK, by urban/rural



Source: Visit Britain, Cebr analysis

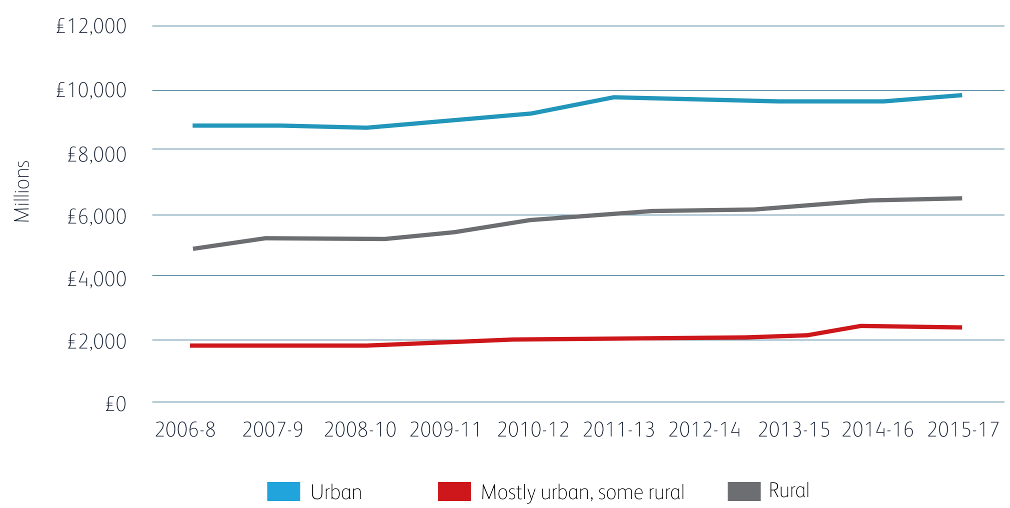
6 http://blogs.lse.ac.uk/brexit/2017/05/26/britains-farmers-get-3bn-a-year-from-the-inefficient-cap-that-has-to-change/

7 Department for Environment Food & Rural Affairs. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/667291/fbs-farmaccountsengland-17july17.pdf

Rural tourism is an immediate area in which communities can diversify beyond agriculture. Data shows that the total trips to rural areas and money spent by visitors has marginally increased since 2014. With the distribution, hotels and restaurants sector already England's third biggest employer in rural areas in 2017, there's potential to magnify the role of these industries further following Brexit.

In the aftermath of Brexit, fluctuation in the value of the pound and uncertainty may hinder holidaymakers going abroad. For those looking to get away, rural areas may be an alternative, particularly for families looking for a break with their children during school holidays and expanding the sector in rural areas could offer opportunities for retail outlets and farm shops promoting rural crafts, among other things.

Figure 7 - Total spend by visitors on trips to the UK, by urban/rural



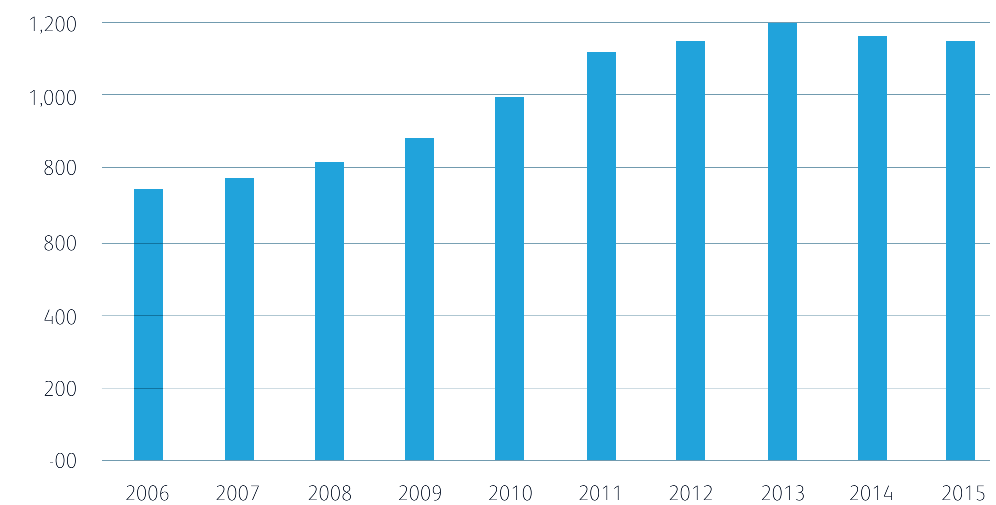
Source: Visit Britain, Cebr analysis

Diversification doesn't have to be limited to just tourism. As well as offering holidays and tourist attractions, some farmers have taken to providing office space, letting their buildings for non-farming use.

Aside from small businesses and start-ups, there's also scope to work with more established sectors in rural areas. Businesses in the professional, scientific and technical sector or in business administration and support services, are among the top five industries in rural areas. Collaboration with these types of businesses could offer potential opportunities in the aftermath of Brexit.

Farmers may find some support in promoting environmentally-friendly initiatives.[8] The Environmental Land Management scheme (ELMS) was announced in the Agriculture Bill currently before Parliament. It's the replacement scheme for current farm subsidies and is aimed at encouraging participating farmers to achieve environmental enhancement and protection, while restoring natural capital and rural heritage. This would include, among other things, schemes to improve air or water quality, habitats for wildlife, preventing climate change or protecting historic features. This financial support will assist farmers in their diversification efforts, making any required adjustments easier.

Figure 8 - UK Ornamental Horticultural produce, (£ Million)



Source: Horticultural Statistics, Cebr analysis

Some farmers could use their land to focus on particular aspects of horticulture post-Brexit. Whilst horticulture involves the production of fruits, nuts and vegetables, it also includes the cultivation, processing and sale of ornamental plants and flowers, as well as additional services, such as plant conservation, soil management and garden design.

Households[9] spent around £7.5bn on garden goods in 2018, with manufacturers selling around £1.3bn worth of garden goods and products. Parks, gardens and green spaces in local areas provided a £131bn aggregate boost to Britain's house prices as part of the appeal of nature. According to a report by the Heritage Lottery Fund, over 90 %[10] of public park managers expect a decrease in their budgets. This provides an opportunity for businesses in the agricultural sector to offer expertise and perhaps land to close the gap. Unlike other parts of agriculture, these horticultural activities do not receive support from the EU's CAP and so will not suffer from the loss of this financial support post-Brexit.

8 Financial Times. https://www.ft.com/content/0ee3cfbe-b5e4-11e8-bbc3-ccd7de085ffe

9 The Horticultural Trades Association. https://hta.org.uk/resourceLibrary/the-economic-impact-of-ornamental-horticulture-and-landscaping-in-the-uk-pdf.html

10 State of UK Public Parks. https://www.heritagefund.org.uk/sites/default/files/media/attachments/state_of_uk_public_parks_2016_final_for_web%281%29.pdf

A report for Irwin Mitchell

Disclaimer

Whilst every effort has been made to ensure the accuracy of the material in this document, neither Centre for Economics and Business Research Ltd nor the report's authors will be liable for any loss or damages incurred through the use of the report.

Methodology

Cebr used its models to forecast employment and gross value added (GVA) growth by local authority in England, and categorised each local authority by Office for National Statistics (ONS) urban or rural classifications. This enabled the forecast of growth rates for three categories of UK regions: 'urban,' 'mostly urban with some rural' and 'rural.'

Authorship and acknowledgements

This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. The views expressed herein are those of the authors only and are based upon independent research by them.
The report does not necessarily reflect the views of Irwin Mitchell

London, April 2019

0370 1500 100 irwinmitchell.com/private