

BRIEFING

A SERIES OF POST-REFERENDUM BRIEFINGS

February 2020

THE OECD SHOWS THAT MR BARNIER (and the UK government) EXAGGERATE THE PERCENTAGE OF UK EXPORTS GOING TO THE EU

DIT, UK Trade in Numbers, February 2020, pp.26-27

Michel Barnier made a statement in Sweden on 9th January 2020 on upcoming trading negotiations, and referred to UK exports to the EU as totalling 43.5% of UK total exports. This was a correct figure taken from UK statistics of gross exports.

However, new publications from the OECD and the UK Department for International Trade [DIT] calculating UK exports in value added terms show that UK exports to the EU in value added terms were 37% of total UK exports (based on 2015 figures, [DIT, UK Trade in Numbers, February 2020, pp.26-27](#)).

Furthermore, considering that almost all the energies on UK-EU negotiations were focussed on goods exports rather than services exports, the UK domestic added value in goods exports to the EU – at risk – is far below this figure.

This is due to:

- Much higher UK domestic added value in service exports than goods exports.
- The Rotterdam effect which only refers to goods exports.
- Some 20% of UK goods exports to the EU are internationally traded items or special items such as raw materials, oil, arms, gold and precious stones, etc.

When this is all accounted for, the UK domestic added value in goods – at risk – exports to the EU falls to under 15% of the UK domestic added value of all UK exports.

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- **Introduction**

In early 2020, there is still talk of the economic ‘catastrophe’ which will be caused to the UK economy by departure from the EU Single Market and the EU generally.

During the three years after the 2016 referendum this possible ‘catastrophe’ had many facets including holdups on the Dover Calais trade route, shortages of imported medicines, suspended air services and forecasts of general economic disorder and falling GDP.

Most of these were never realistic scenarios and there is now concentration on one possible realistic area, which is, that the UK’s exports to the EU will be badly reduced by trade and non-trade barriers on leaving the Single Market.

Nor is this concern without merit. It will be difficult and, in some areas, impossible to retain the previous ‘frictionless’ trading arrangements with the EU27 and, to a lesser extent, with the other EEA countries. Another matter which needs even closer attention is to replace the trade arrangements, which the UK benefited from as part of the EU’s trade agreement, with other countries.

Equally, internationally traded or special items such as raw materials, oil, armaments, gold and precious stones, etc. will likely be unaffected.

Therefore, to understand what difficulties might arise, it is necessary to examine closely exactly what trading relationship to UK has and had with the Single Market especially as regards UK exports.

- **Gross trade statistics are not the whole story**

Statistics of gross trade exports tell us little since they are only a compendium of all sorts of goods and services. Some of these, such as gold or re-exports, may add to the total of gross UK exports but add little to UK domestic added value whether in wages or return to capital. Others have much imported value added.

The key point about all trade transactions is that not all trade is of equal value and this is especially true of the UK economy where a lot of exports are services with a high level of UK domestic added value. It is UK domestic added value that matters, not gross export statistics.

New publications from the OECD and the UK Department for International Trade, show that UK exports to the EU27 are much less important in value added terms than in gross export statistics. Indeed, when the UK domestic added value in service exports to the EU is stripped out, the UK domestic value added in UK goods exports to the EU is relatively small.

- **Trade in added value**

[The latest publication by the Department for International Trade \(February 2020\) of ‘UK Trade in Numbers’](#), pp.26-27, has a new statistical resource and is compiled from OECD published value added trade figures for 2015. (The tables are attached as Appendix 1 to this Briefing.)

This shows considerable differences, looking at UK exports and UK-EU exports in particular, when considering gross trade figures and value added trade figures (note these figures all refer to total exports of goods and services)

The OECD/DIT publication calculates that 84.9% of UK gross exports contain domestic added value, 6.6% contains value added by the EU 27 and 8.5% is value added by non-EU countries.

This is complemented by a table considering and comparing the top 5 UK export markets (in 2015) in gross terms and in value added terms.

The most striking figures in the table are that exports to the EU, which comprise 43.5% of UK exports in gross terms (this exact figure was again stressed by Michel Barnier in his statement of 9/1/20 in Sweden), amount to only 37.0% in value added terms. This is a big difference.

A good part of the difference is accounted for by trade to Ireland which falls from 5.9% in gross terms to 3.4% in value added terms.

Irish trade statistics are themselves markedly affected by the figures of US conglomerates operating in Ireland.

The counterpart of the UK's exports being considered in value added terms is that, with the EU share being diminished, exports to the Rest of the World rise from 56.50% to 63% of total UK exports. The share of exports to the USA rises from 15.7% to 17.9%.

If the OECD/DIT figures shown in the two tables from *UK Trade in Numbers* are correct, that while UK gross exports to the EU were 43.5% of UK total exports in 2015 but only 37% in value added terms, it is worth considering how this came about. In 2015 services were 40.6 % of UK Gross exports to the EU while they were 50.01% of UK gross exports to the Rest of the World. Thus a higher ratio of 9% in the proportion of services to total trade and 9% less in the proportion of goods to total trade raised the proportion of value added to the Rest of the World from 56.50% to 63%, an increase of 6.5%. Quite stunning figures.

Of course, there could be explanations such as that there are sales of higher value services outside the EU or, indeed, higher value goods are sold outside the EU, thus adding higher UK domestic added value. These seem unlikely explanations and the fact remains that UK domestic value added is much higher in trade with the Rest of the World than with the EU and this is connected with a higher ratio of services to goods in the relevant total exports.

- **A short history of Value Added Trade**

The OECD and the WTO started an examination of value added trade data around ten years ago. At first they were mainly interested in the actual value of Chinese exports. They recognized that there was double counting in the gross exports' figures normally presented by national data because gross exports also

contained items exported by other countries and so, for example, in China the Apple mobile phone contained about 90% of its value from parts imported into China which were then exported, so appearing in both the import and export side of Chinese data.

This problem in trade data has always been recognized but in the past the relative smallness of the quantum of imported parts then re-exported was such that it made the trade deal gross export figures data untidy but still meaningful. The tide of globalization changed that and with international trade being dominated by multi-nationals drawing on components and supplies from many other countries, the old gross exports statistics became out of date.

A further point was the growth in services' trade which generally had high domestic value added and were, therefore, economically valuable in value added terms. The US and UK are by far the world leaders in this area and the underestimation of the value of service trade provided an explanation for the apparent ability of these countries to run large gross goods' deficits interminably.

The OECD with the WTO spent a great deal of time and energy to produce a Worldwide analysis of value added trade and this throws up some surprising data now incorporated by the UK Department for International Trade's Bulletin in September 2019 although this was based on 2015 figures.

Value added trade is also considered, at some length, in the DIT's publication (*Trade and Investment Core Statistics Book, last updated 17 December 2019*). *Core Statistics* makes it clear that the trade in value added statistics is still an experimental dataset. *"Data limitations mean that TIVA (Trade in Value Added) should be considered as complementary to analysing Trade patterns rather than a replacement of traditional trade statistics."*

Nevertheless it concludes that:

- a) *"The import content of UK exports was 15.1% in 2016 significantly below the OECD average of around 26%."*
- b) *"The UK's relatively low import content partly reflects its specialization in Services exports which tend to have low import content."*
- c) Key Finding: importance of services

"TIVA data shows that services are more important to UK exports than they appear in traditional trade statistics. According to the ONS Pink Book (2018) services represented around 46% of UK exports in 2016. But according to TIVA, the share is significantly higher (around 71%). This is one of the highest among the countries in the OECD dataset, with significant services content embedded in manufacturing exports (32% in 2016)."

Note: Embedded services in manufacturing are treated as manufacturing as regards tariffs and quotas, etc.

d) *"The USA is the UK's top export market in both gross and value added terms ... In value added terms, the importance of the USA as an export market is amplified, with a share of 17.9% while the EU becomes a less important export market (with a share of 37%, compared to 43.5% in gross terms)".*

e) *"In value added terms ... the USA becomes the largest import services source (13.4%) ahead of Germany (11.4%) and China (9.5%). The EU becomes a less important market in value added terms (accounting for 45.5% of total UK imports) compared to 51% in gross terms."*

While this paper does not discuss value added in imports, this change of figure is worth noting.

- **With the UK having a large part of its exports in services, none of this is surprising to those who have commented on this in the past**

There are two phenomena.

First, the percentage of services to total exports is higher in trade with the Rest of the World than with the EU27. Thus the value added in Rest of the World sales is greater than apparent gross exports to the Rest of the World.

Second, considering only UK exports to the EU the value added of services in percentage terms is greater than in the apparent gross exports to the EU27.

It is normally a function of 'services' trade that it generates high domestic value added figures.

- **The Rotterdam effect**

According to the ONS study *'Who does the UK trade with?'* of 3rd January 2018, *"The Rotterdam effect is the situation where goods which are initially exported to one country are then re-exported somewhere else. An ONS article estimated that 50% of all exports to the Netherlands were re-exported to non-EU countries. It also estimated that the Rotterdam effect would account for around four percentage points of the UK's export of goods"*. This is about 2.5% of total UK exports to the EU27. [The ONS wording is a little obscure here]

Four percentage points of the UK's exports of goods in 2015, which totalled around £285 billion, is £11.2 billion.

This reduces UK domestic added value in goods exports to the EU by approximately 2.5% and adds 2.5% to UK domestic added value of goods exports to the Rest of the World by 2.5%.

The Rotterdam effect also affects UK trade figures for exports to Belgium as Antwerp also serves as a major transshipment site for worldwide trade.

Recently an academic at Erasmus University noted on considering both re-exports and goods in transit, "This means a hard Brexit will be less severe than

the Remain- camp claims. The costs will be 8/9 percent lower than they estimated.”

- **What has happened since 2015**

The phenomena have grown more by 2018.

Services exports to the Rest of the World had slightly increased as a percentage of total exports to the Rest of the World.

Considering only UK exports to the EU, the percentage of services exports to the EU compared with total exports to the EU had also slightly increased in four years.

Both these phenomena indicate that it is likely that, in value added terms, the relative importance of the EU market to UK exports has declined further in value added terms from the 37% estimated in 2015 or 34.5% after taking account of the Rotterdam effect.

- **The Negotiations**

Taking account of these two statistical analyses (and there are others mentioned by the ONS, such as the Gold trade), it would appear that, in value-added terms, and that is ultimately what counts, the EU share of total UK exports could be re-stated as:

Gross exports' calculation for 2015	43.5%
<u>Less:</u> Change to value added basis	(6.5%)
Rotterdam effect	<u>(2.5%)</u>
Value added calculation for 2015	34.5%

The consequence is that in 2015, in value added terms, the share of UK exports outside the EU is 65.5%.

This analysis is not an attempt to minimize the importance of UK exports to the EU. Rather it emphasizes the importance of Service exports where there is high domestic added value. Yet the future structure of services trade with the EU after Brexit has barely been discussed.

A quick deal on trade in goods is highly advantageous to the EU. While what is of great importance for the UK negotiators is to preserve the ability of the UK to maintain and increase its services trade with the EU and, indeed, the Rest of the World.

Mark Carney, the soon-to-be outgoing Governor of the Bank of England, is reported on 8th January 2020 as stating to the Financial Times: *“It is not desirable at all to align our approaches, to tie our hands and to outsource regulation and effectively supervision of the world’s leading complex financial system to another jurisdiction”*. On the whole, EU27 exports of services to the UK are very concentrated on business services and travel. That is why Spain features very highly. It is difficult to see any advantage in seeking alignment in the direction of the EU27 when it is a minor player in most service areas.

The UK domestic added value in services exports is, quite evidently, what is the most valuable benefit of trade for the UK.

As can be seen in Appendix 2 of extracts from the 2019 Pink Book, the ratio of service exports to goods exports in UK exports to the Rest of the World is about 50% while it is about 41% for exports to the EU.

Domestic value added content is generally much higher in services exports.

Not all trade is of the same value to the trader.

- **Conclusion**

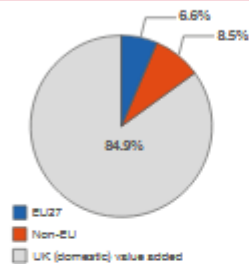
What is unknown is the exact percentage of UK domestic added value content in services and/or in goods.

Taking 2015 figures of UK services exports to the EU of £91,304 billion and goods exports of £133,245 billion and reducing this latter by £11.2 billion for the Rotterdam effect, it seems a reasonable starting point that goods exports and service exports to the EU add about 50% each in total UK domestic added value in exports to the EU. Thus the value added in goods exports to the EU is some 17% of the total UK domestic value added in all UK exports. As around 20% of UK goods exports are in internationally traded goods, this figure reduces the UK domestic added value – at risk – in goods exports to the EU to about 13.5% of total UK domestic added value in total UK exports.

This is certainly an amount well worth negotiating as hard as possible to retain. If negotiations are about goods, the actual headline figure for the quantum of UK domestic added value in exports to the EU – at risk – is more likely 13.5%.

Of course that does not mean that 13.5% of UK added value exports would be lost in the event of a complete breakdown in trade between the EU and the UK. It is simply the total percentage of all UK added value exports which go to the EU27 and which are not services, internationally traded goods or onward exports to extra EU destinations.

Origin of value added in UK gross exports (2015)



UK exporters are slightly more dependent on Non-EU suppliers for the production of their exports (2015).

EU27	6.6%
Germany	1.8%
France	1.1%
Italy	0.6%
Ireland	0.5%
Spain	0.5%
Netherlands	0.5%
Belgium	0.3%
Sweden	0.2%
Poland	0.2%
Denmark	0.1%
Other	0.7%

Non-EU	8.5%
United States	2.1%
China	1.2%
Norway	0.7%
Japan	0.4%
Russia	0.4%
Canada	0.4%
India	0.3%
Switzerland	0.3%
Turkey	0.2%
South Korea	0.2%
Other	2.3%




The strongest backward linkages are with the United States, China and Norway (from the Non-EU) and Germany and France (from the EU27).

Source: OECD TIVA December 2018








Top 5 export markets in gross and value added terms (2015)

Top 5 export markets for the UK in 2015

Gross data

	Partner	% of total exports
1	 United States	15.7%
2	 Germany	8.1%
3	 France	6.6%
4	 Ireland	5.9%
5	 China	4.6%
	 EU	43.5%
	 World	100.0%

Value added data

	Partner	% of total exports
1	 United States	17.9%
2	 Germany	7.8%
3	 France	6.5%
4	 China	5.6%
5	 Ireland	3.4%
	 EU	37.0%
	 World	100.0%

The United States was the UK's largest export market in both gross and value added terms in 2015.

In value added terms, the importance of the United States as an export market is amplified, with a share of 17.9%, while the EU27 becomes a less important export market (with a share of 37.0%, compared to 43.5% in gross terms).

Source: ONS TMA December 2015

APPENDIX 2: The Statistics

UK Exports in £ Gross Exports

[Extracts from the 2019 Pink Book]

Year	Total Services Exports to EU28	% Services to Total Exports	Total Goods Exports to EU28	Total Goods & Services Exports to EU28
2015	91,304	40.6	133,245	225
2016	105,629	42.7	142,275	247
2017	117,048	41.8	163,850	280
2018	120,283	41.33	170,705	291
Year	Total Services Exports to Rest of World	% Services to Total Exports	Total Goods Exports to Rest of World	total Goods & Services Exports to Rest of World
2015	152,785	50.01	152,715	305,500
2016	163,948	51.31	155,547	319,495
2017	174,571	50.13	173,616	348,187
2018	177,136	50.43	174,106	351,242
Year	Total Services Exports to World (EU plus ROW)	% Services to Total Exports	Total Goods Exports to World (EU PLUS row)	Total Goods & Services to World (EU plus ROW)
2015	244,089	46.05	285,960	530,049
2016	269,577	47.54	297,922	567,499
2017	291,619	46.34	337,466	629,085
2018	297,419	46.32	344,811	642,230