Policy Contribution
Issue n˚18 | 2016

What consequences would a post-Brexit China-UK trade deal have for the EU?

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This Policy Contribution is a contribution to a research project on EU-China relations undertaken by Bruegel, CCIEE (China Centre for International Economic Exchanges), Chatham House and the Chinese University of Hong Kong.

Executive summary

BREXIT MEANS THAT the United Kingdom could be able to run its own trade policy, which opens the door for the potential negotiation of a free trade agreement between the UK and China. We ask three questions about this important issue for the UK-EU economic relationship. If a China-UK FTA was signed, could Chinese exporters break into the EU market through the UK, making a possible China-EU FTA relatively superfluous? Would a China-EU FTA help UK exporters to gain a competitive advantage in China relative to EU exporters? Will UK producers benefit by importing cheaper Chinese intermediate goods?

OUR ANALYSIS INDICATES that a UK-China FTA will be neither easy nor clearly advantageous for the UK. First, it will be difficult for the UK to reach an agreement with China without first establishing a new post-Brexit partnership with the EU. Negotiating tariffs with other WTO members will be a pre-condition if the UK exits the EU customs union, and this process will require time and effort. Second, even if the UK reaches an agreement with China, the UK cannot serve as a back door for Chinese products to enter the EU, because the EU is very likely use rules of origin to close any such loopholes. In addition, entering the EU via the UK will entail an additional transportation cost for Chinese goods that will, at least partly, offset any tariff savings, making use of such a loophole less worthwhile. Third, the UK and the other EU economies differ in most of their exports to China, so there would be very limited substitution between them.

IT THEREFORE SEEMS that establishing a new trade relationship with the EU would be a more urgent task for the UK in the post-Brexit world, rather than an FTA with China. Under such circumstances, the UK might need to postpone its trade negotiations with other economies outside of EU, including China. This goes beyond the current discussion of the illegality of the UK starting to negotiate trade deals before it leaves the EU. The issue is whether it makes economic sense for the UK to do so, and the answer is no. In fact, the more the UK reaches an independent favourable trade agreement with China after Brexit, the harder it will be for the UK to strike a good deal with EU. In the meantime, it is also urgent for the UK to negotiate with the main WTO members on tariffs, because outside the EU, the UK might not participate in the EU schedule of concessions. The best strategy for the UK would be to negotiate with the other WTO members with the EU-based tariffs as a starting point, to avoid negotiating over terms separately and also to maintain a close relationship with the EU.

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1. Introduction

Brexit means that the UK could be able to run its own trade policy, which opens the door for the potential negotiation of an FTA between the UK and China.

The United Kingdom has for long time flirted with the idea of establishing a free trade agreement (FTA) with China. Already in December 2013, during an official visit to China, the then UK prime minister David Cameron claimed he could act as a catalyser for an EU-China trade deal. Such a statement was not well received in Brussels, given the Commission's sole responsibility for trade policy at the EU level. Furthermore, the mood in Brussels was that the EU-China economic relationship was not yet balanced enough to engage in FTA negotiations[1].

Brexit has obviously drastically changed this picture. Brexit means that the UK could be able to run its own trade policy, which opens the door for the potential negotiation of an FTA between the UK and China. However, the UK still faces a number of constraints.

First, if Brexit means that the UK would no longer enjoy the EU's schedule of concessions for goods with the World Trade Organisation, the UK would be obliged to negotiate a fresh schedule of concessions before any bilateral FTA. This negotiation would not be as simple as it might seem because its outcome would require the consent of all WTO members. In reality, some WTO members might want to gain more favourable terms given that the UK would have less negotiating power, its economy being four times smaller than the rest of the EU[2]. All in all, the process before the UK could conclude FTAs with countries such as China would be full of uncertainties, and most importantly, would be time consuming.

Second, even if the UK were to resolve the WTO-related hurdles and could technically start to negotiate an FTA with China, the type of trade partnership that the UK might eventually want to shape with the EU would be bound to have a bearing on its negotiations with China. The more the UK retains its EU trade ties through its FTA with the EU, the harder it will be to do the same with China. It should be noted in this regard that even those campaigning for the UK to leave the EU favour maintained access to the EU market through an FTA. Their real problem was the labour mobility aspect of the single market[3].

In the baseline scenario that the UK will pursue a trade agreement with the EU[4], the question then is how the UK will pursue an FTA with China in parallel.

We break down this important issue for the UK-EU economic relationship by asking three key questions. First, if an FTA between China and the UK were to be signed, would it be possible for Chinese exporters to break into the EU market through the UK, making a possible FTA between the EU and China relatively superfluous? Second, would such an FTA between the UK and China help UK exporters to gain a competitive advantage in China and replace the EU's exports? Third, will UK producers benefit by importing cheaper Chinese intermediate goods and thus gain competitiveness relative to the EU?

By addressing these questions in turn, we conclude that a China-UK FTA would have a very limited impact on the EU's imports. However, it would affect the EU's exports although in a very asymmetric way for different EU member states.

1 See *Euractiv* (2013) 'Cameron irritates Brussels by pushing EU-China trade deal', 3 December, available at https://www.euractiv.com/section/uk-europe/news/cameron-irritates-brussels-by-pushing-eu-china-trade-deal/. Also see the European Commission (2016) 'Elements for a new EU strategy on China', available at http://europa.eu/rapid/press-release_MEMO-16-2258_en.htm.

2 André Sapir (2016) 'Should the UK pull out of the EU customs union?', *Bruegel Blog*, 1 August, available at http://bruegel.org/2016/08/should-the-uk-pull-out-of-the-eu-customs-union/.

3 Sam Ashworth-Hayes (2016) 'We won't be in single market without free movement', *InFacts*, 6 April, available at https://infacts.org/mythbusts/uk-wont-single-market-without-free-movement/.

4 *BBC News*, 'Five models for post-Brexit UK trade', http://www.bbc.com/news/uk-politics-eu-referendum-36639261.

2. The UK 'back door': no easy way for Chinese exporters to use the UK to enter the EU market

What would be the consequences for the EU of China signing an FTA with the UK while the UK maintains at least an FTA with the rest of Europe, if not full participation in the single market? This 'status quo' scenario should raise concerns for the EU about whether Chinese exports could use the UK 'back door' to enter the EU market without China signing a bilateral FTA with the EU. The answer really depends on what type of trade agreement the UK and the EU reach following Brexit.

The irony of a push by the UK to rush into an agreement with China is that it could make it harder for the UK to retain full access to the EU single market.

If the UK were to maintain EU single market status, there would be virtually no inspections of products transferred from the UK to other EU countries. In this circumstance, a favourable FTA between China and the UK would become a true back door for Chinese products to enter the EU market. The irony of this push factor for the UK to rush into an agreement with China is that it could actually make it harder for the UK to retain full access to the EU single market, with an outcome that would probably be more costly (surely as far as financial services are concerned) than the gains from an FTA with China. There is however a halfway option, as illustrated by the Swiss example. Switzerland is not in the EU but has reached a number of FTAs with the EU in the context of the European Free Trade Association (EFTA). At the same time, Switzerland has also established FTAs with 38 partners outside the EU, including China[5]. To prevent non-EU imports from entering the EU market through Switzerland, the EFTA states such as Switzerland must apply rules of origin that show to what extent a certain good is produced and processed within the European Economic Area (EEA) in order to enjoy preferential tariffs, otherwise normal tariffs apply[6]. The same type of rule has also been included in the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada, which is yet to come into force[7]. Following these precedents, it is very likely that the EU would apply rules of origin to the flow of goods between the UK and the EU. These measures will thus make it difficult for Chinese corporates to use the UK back door to enter the EU market.

In addition, international transportation of goods from China through the UK to EU countries will be handicapped by additional transportation costs. Goods sent from China to Europe mainly travel by sea, with maritime transportation accounting for nearly 60 percent of China's international trade[8]. Unlike air or road transportation, long-distance maritime transportation must follow specific routes to minimise time and costs. Table 1 lists the main shipping routes from China to Europe, as provided by the China Ocean Shipping Company (COSCO), a major Chinese global carrier company. Most container ships from China to Europe dock at the ports of Antwerp, Hamburg and Rotterdam, with more limited volumes going through Felixstowe and Southampton in the UK (Table 1). As Felixstowe and Southampton, two of the UK's major ports for Chinese ships, only rank as the seventh and seventeenth busiest container ports in Europe (Table 2), their cargo-handling capacities

5 See the introduction of the Switzerland trade agreements, http://www.s-ge.com/switzerland/export/en/content/static/Free-Trade-Agreements. A current overview of Swiss trade agreements can be found at: https://www.seco.admin.ch/seco/en/home/Aussenwirtschaftspolitik_Wirtschaftliche_Zusammenarbeit/Wirtschaftsbeziehungen/Freihandelsabkommen/Liste_der_Freihandelsabkommen_der_Schweiz.html.

6 See EFTA, 'Free Movement of Goods,' http://www.efta.int/media/publications/fact-sheets/EEA-factsheets/Goods-FactSheet.pdf.

7 Also see *BBC News*, 'Five models for post-Brexit UK trade,' http://www.bbc.com/news/uk-politics-eu-referendum-36639261.

8 See Alicia Garcia Herrero and Jianwei Xu, 'China's Belt and Road Initiative: Can Europe expect any trade gains?,' http://bruegel.org/2016/09/chinas-belt-and-road-initiative-can-europe-expect-trade-gains/

is relatively limited. Therefore, detours for goods from China via the UK before they enter other EU countries would be not realistic in the short run. Even if the handling capacity of UK ports is increased in the future, a company using the UK as a back door to the EU would incur a non-negligible transportation cost to their final destination, whether by maritime or other transportation modes. According to our calculation, based on the World Input-Output (WIOD) database, the share of international transport costs in total inputs for both intermediate and final goods is approximately 4 to 5 percent for most EU countries (Figure 1), while the average Most Favoured Nation (MFN) rate for Europe is already as low as 1.5 percent[9]. Therefore, in international trade terms, transportation costs seem to be more important than tariffs. Thus, the additional transportation cost of a detour via the UK for Chinese goods destined for the EU would at least partly offset the intended tariff saving to make the UK back door a less profitable choice.

In international trade terms, transportation costs seem to be more important than tariffs.

Table 1: COSCO European and Trans-Atlantic service routes

COSCO's main route service codes	European ports
Asia-Mediterranean Route	
AMX8	Malta, Rijeka, Koper, Trieste, Venice
BEX	Piraeus, Ambarli, Constanze, Odessa
FEM	Piraeus
AMX1	La Spezia, Genova, Fos, Valencia
MD1	Piraeus, Genoa
MD2	La Spezia, Genova, Fos, Valencia
MD3	Malta, La Spezia, Genova, Valancia
MEX1	Malta, Fos, Barcelona, Valancia
Asia-North Europe Route	
AEX1	Felixstowe, Rotterdam, Hamburg
FAL1	Algeciras, Dunkirk, Southampton, Felixstowe, Rotterdam, Hamburg
FAL3	Le Havre, Antwerp, Rotterdam, Hamburg, Felixstowe
NE2	Piraeus, Antwerp, Rotterdam, Hamburg, Felixstowe
NE3	Antwerp, Rotterdam, Hamburg
NE5	Rotterdam, Hamburg, Felixstowe
NE6	Algeciras, Rotterdam, Hamburg
NE7	Piraeus, Antwerp, Rotterdam, Hamburg, Felixstowe

Source: Bruegel based on China Ocean Shipping Company (COSCO), http://www.coscon.com/, as of 27 September 2016.

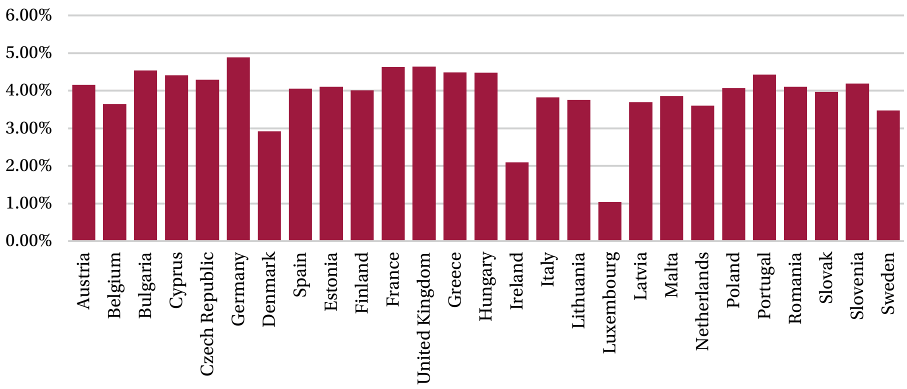
9 The statistics for tariffs are taken from the World Bank WDI database. The applied weighted average tariffs for the European Union are 1.09 percent, 1.02 percent, 1.04 percent and 1.51 percent from 2011 to 2014.

Table 2: Europe's busiest ports

Rank in Europe	Port	State	1000 TEU (Twenty-feet equivalent units, 2014)
1	Rotterdam	Netherlands	12,298
2	Hamburg	Germany	9,729
3	Antwerp	Belgium	8,978
4	Bremerhaven	Germany	5,796
5	Algeciras	Spain	4,555
6	Valencia	Spain	4,442
7	Felixstowe	United Kingdom	3,700
8	Piraeus	Greece	3,585
9	Ambarli/Istanbul	Turkey	3,600
10	Gioia Tauro	Italy	2,970

Source: Report from the Port of Rotterdam. https://www.portofrotterdam.com/en/files/top-20-european-container-ports.

Figure 1: International transport costs, share of total foreign inputs



Source: Bruegel based on WIOD database.

3. An FTA with China would benefit the UK in the Chinese market, particularly for the 'motor cars and vehicles' sector

If a China-UK FTA was reached, the UK would undoubtedly gain competitive advantage in terms of access to the Chinese market.

China is the second largest destination for EU exports, accounting for 9.5 percent of the EU's total exports. If a China-UK FTA was reached, the UK would undoubtedly gain competitive advantage in terms of access to the Chinese market. Would the improved UK-China economic collaboration affect the EU's exports?

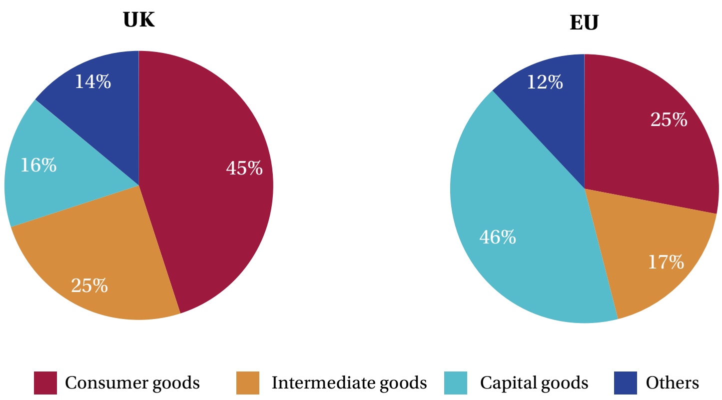
To understand the possible implications of a China-UK FTA, it is straightforward to compare the EU's and the UK's export structures. Figure 2 decomposes the UK's exports into capital goods, consumer goods, intermediate goods and raw materials, and compares them to those of the rest of the EU[10]. Consumer goods constitute the largest share of the

10 To do this, we use a concordance from WITS: http://wits.worldbank.org/referencedata.html.

UK's exports to China (45 percent), followed by intermediate goods (25 percent), whereas the consumer goods share for the rest of the EU is 25 percent and the intermediate goods share is only 17 percent. The EU mainly exports capital goods to China, with a share of 46 percent of total exports, but the capital goods share makes up only 16 percent of the UK's total exports to China. In this sense, the UK's export composition is distinctly different to that of the rest of the EU.

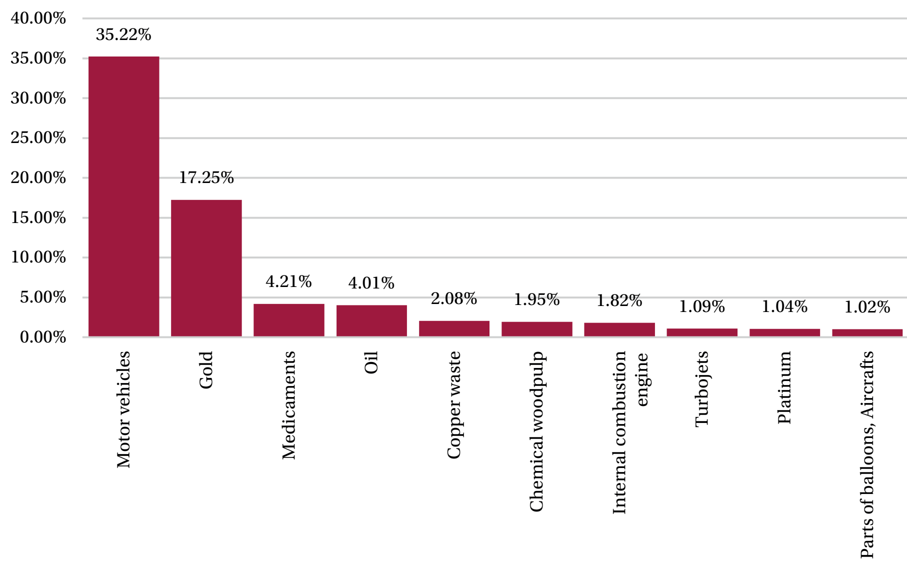
We next move to the product structure of the UK's exports in comparison to those of other EU countries. Figure 3 reports the UK's top ten product categories exported to China. These products constitute 70 percent of the UK's exports to China. In Table 3, we compare these top exports to those of the UK's major competitors in the EU. To see the potential of a China-UK FTA, we also report the current MFN tariffs for these products.

Figure 2: Composition of exports from the UK and the rest of the EU to China



Source: Bruegel.

Figure 3: The UK's top ten exports to China as a % of EU exports to China in each category



Source: Bruegel based on the OECD bilateral database.

If the UK were to continue to have single market access, a China-UK FTA could harm other EU countries' competitiveness in the automobile sector.

The most important export category from the UK to China is 'motor cars & vehicles'[11], which alone accounts for 35.2 percent of the UK's exports to China. The major competitor

11 We use HS4 product classifications for analysis. All the terms are shortened for ease of reading.

to the UK in this category is Germany, whose exports make up more than 50 percent of the EU's total exports in this product category. The auto category is also important for Slovakia. Although its share is only 5.23 percent, it is nonetheless an important industry given that it is the country's largest industry and accounts for 12 percent of its GDP[12]. Because the current importing MFN rate to China is 25 percent, once the UK strikes an FTA with China, UK exporters in this category could expect a big cut to their bilateral tariffs.

However, this trade benefit might be less promising than it seems. Most UK car manufacturing is foreign owned, and its continued presence in the UK could be very dependent on the UK keeping or losing its single market membership. If the UK exits the single market, these foreign investors could divert their investment to other EU countries, minimising the impact of a UK-China trade deal. Instead, if the UK were to continue to have single market access[13], a China-UK FTA could harm other EU countries' competitiveness in the automobile sector, with Germany and Slovakia being especially affected.

Table 3: UK share of EU exports to China compared to its main EU competitors, selected categories

	Motor cars & vehicles	Gold	Medicaments	Crude oil	Copper waste and scrap	Chemical wood pulp	Internal combustion engines	Turbojets and turbopropellers	Platinum	Parts of balloons, aircraft, spacecraft
Belgium	4.10%	0.00%	8.47%	0.00%	5.92%	6.76%	0.57%	1.08%	5.57%	0.79%
Germany	51.67%	0.10%	23.41%	0.00%	20.71%	3.07%	40.10%	8.57%	42.22%	54.85%
Spain	0.04%	0.00%	2.71%	0.00%	7.04%	7.62%	0.15%	0.13%	0.00%	0.92%
France	0.57%	0.03%	10.11%	0.00%	5.45%	5.80%	2.25%	61.76%	0.01%	20.69%
United Kingdom	**29.21%**	**99.87%**	**17.54%**	**99.98%**	**22.66%**	**45.82%**	**44.80%**	**14.51%**	**46.04%**	**18.74%**
Italy	3.11%	0.00%	10.20%	0.00%	6.75%	11.49%	3.60%	6.01%	6.04%	0.92%
Netherland	0.47%	0.00%	2.92%	0.00%	19.03%	17.05%	0.46%	2.80%	0.02%	0.74%
Slovakia	5.23%	0.00%	0.00%	0.00%	0.10%	0.00%	0.00%	0.00%	0.00%	0.01%
Sweden	0.85%	0.00%	12.75%	0.00%	1.92%	0.03%	4.50%	0.80%	0.07%	0.04%
MFN tariffs	25.00%	0.00%	5.11%	0.00%	0.00%	0.00%	8.26%	2.67%	0.75%	0.75%

Source: Bruegel.

Another potentially important product category is 'internal combustion engines', which ranks as the UK's seventh most valuable export category to the Chinese market. The UK and Germany compete strongly in this sector, with each taking more than 40 percent of EU market share in China. Given that the MFN tariff for the product is 8.26 percent, a possible China-UK FTA would also facilitate the UK's competitiveness in China and could have some negative effect on Germany.

The spillover effects for the other products are expected to be small. The UK's second largest export product is 'gold', making up more than 17 percent by value of the UK's exports to China. However, because the MFN tariff for this product in China is zero, there is already no room for further reduction.

The third largest product category is 'medicaments', which makes up 4.51 percent of the

12 'Automotive industry in Slovakia', https://en.wikipedia.org/wiki/Automotive_industry_in_Slovakia.

13 Similarly to Norway, which through the European Free Trade Association can sign trade deals with other countries.

UK's exports to China. Although there are several countries competing in this product category, including Belgium (8.47 percent share of EU exports to China in this category), Germany (23.41 percent), France (10.11 percent), Italy (10.20 percent) and Sweden (12.75 percent), the current MFN tariff rate is 5.11 percent and there would be limited room for tariff reduction. As such, a China-UK FTA would only have a moderate effect on this product category.

The UK's next three top export products, 'crude oil,' 'copper waste and scrap,' and 'chemical wood pulp,' make up a significant share of the EU's exports to China. However, the MFN rate is again zero percent, so there would be no spillover effect arising from the China-UK FTA. For the UK's other top export products, the MFN tariff is also very low, so the possible FTA would offer little gain to the UK's firms on the Chinese market.

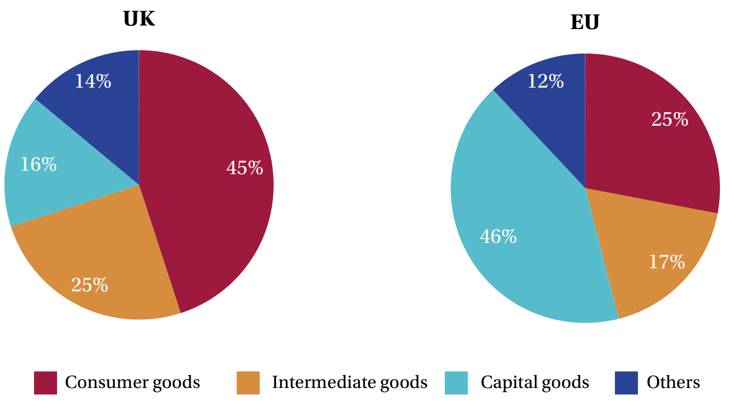
All in all, if the UK can maintain some form of single market status with the EU, a China-UK FTA could be expected to produce huge benefits in favour of the UK's 'motor cars & vehicles' sector. This would undoubtedly have a significantly negative influence on German and Slovakian auto exports to China. In addition, German export sales of the product category 'internal combustion engines' would be jeopardised. For the rest of the product categories, the spillover effect would be moderate at most.

4. The reduced costs of UK imports, thanks to an FTA with China, would be at most moderate

The UK's imports from China are also mostly concentrated on consumer goods. Within the EU, the UK is after Germany the second largest end importer of consumer goods from China. Consumer goods from China account for more than half of the UK's total imported goods from China by value (53 percent). In comparison, the values of capital and intermediate goods are 22 percent and 16 percent respectively of the UK's imports from China, below the average level for the rest of the EU.

Consumer goods from China account for more than half of the UK's total imported goods from China by value (53 percent).

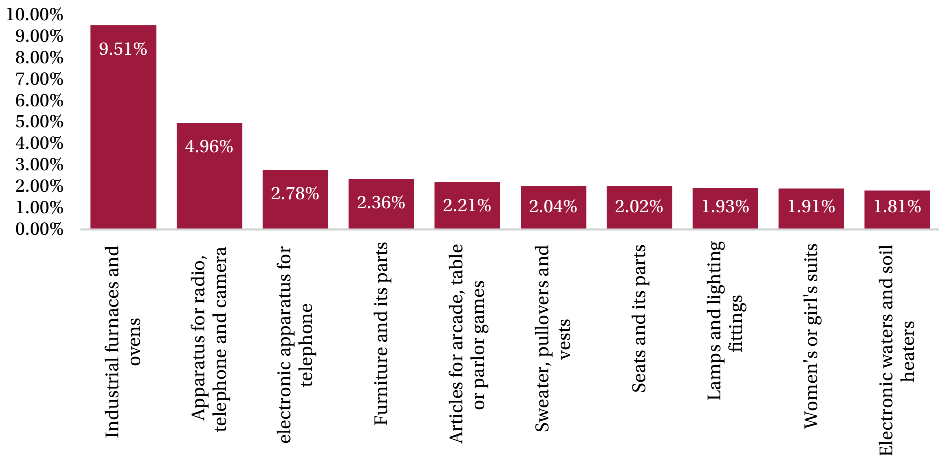
Figure 4: Capital, intermediate and consumer goods imported from China by the UK and the rest of the EU



Source: Bruegel.

Although the UK relies more on consumer goods in its imports from China, the distribution of these goods is broad based. Even the largest consumer goods category, 'furniture and its parts,' makes up only 2.36 percent of China's exports to the UK. Therefore slicing tariffs would have differing impacts across a variety of consumer goods categories, depending on the specific tariffs that currently apply. The second column of Table 4 reports the related MFN tariffs for the UK's top five categories of consumer goods imports from China. It can be seen that the greatest impact might come from 'sweaters, pullovers and vests', for which the current MFN tariff reaches nearly 12 percent. But for the other sectors, the MFN tariffs are quite limited so the benefit from an FTA would be small. This is especially so for the 'lamp and lighting fittings' category for which the MFN tariff is already zero percent so there would be no possible effect arising from an FTA. As such, an FTA could be only relevant for specific consumer goods sectors.

Figure 5: The UK's top ten imports from China, as % of total imports from China



The distribution of capital goods is more concentrated. Figure 5 shows that the top three product categories that the UK imports from China, 'industrial furnaces & ovens, non-electronic products' (9.51 percent) , 'apparatus for radio, telephone and camera' (4.96 percent), 'electronic apparatus for telephone' (2.78 percent), are all capital goods. However, for these three product categories, the average MFN tariff rates are 0.00 percent, 2.90 percent and 0.00 percent respectively, implying that there would be nearly no potential for these major capital goods from further reductions in tariffs.

Table 4: MFN tariffs for UK's top five imported consumer, capital and intermediate goods categories from China

Consumption goods		Capital goods		Intermediate goods	
Product	*MFN tariff rate*	*Product*	*MFN tariff rate*	*Product*	*MFN tarriff rate*
Furniture and its parts	1.66%	Industrial furnaces and ovens, non-electric, parts thereof	0.00%	Festive arts	2.03%
Articles for arcade, table or parlor games	3.70%	Apparatus for radio, telephone and camera	2.90%	Iron and steel parts	0.00%
Sweater, pullovers and vests	11.91%	Electronic apparatus for telephone	0.00%	Flat-roll iron and steel	0.00%
Seats and their parts	2.98%	Semiconductor devices, light-emit diodes etc, parts thereof	0.00%	Knitted or crocheted fabrics	14.50%
Lamps and lighting fittings	0.00%	Parts etc for typewriters & other office machines, computer assessorial	0.33%	Bars and rods	0.00%

Intermediate goods have received global attention in modern international trade. Undoubtedly the reduction in tariffs can have certain implications for sectors that depend more on imported intermediates. The UK's Brexit minister David Davis has argued that an FTA with China will reduce the intermediate cost of car components and increase the UK car sector's global competitiveness. However, according to our estimates, only eight percent of the UK's imports from China fall into the intermediate goods category, so the final effect is expected to be small. The last column of Table 4 shows the MFN tariffs for the UK's top intermediate goods imports from China. It can be seen that the MFN tariffs for most products in this category are already very low. Though there are very high rates for certain categories, such as 'knitted and crocheted fabrics', the trade volumes for these product categories are low, making up less than one percent of the UK's total imports. In particular, the MFN tariff for the parts and accessories of motor vehicles is as low as 3.81 percent. Against this backdrop, even if China and the UK succeed in striking a zero-tariff agreement for these intermediate goods, the impact on the price of final goods would be far less than four percent. Therefore, a China-UK FTA would have very moderate impact, if any, on the UK's global competitiveness from the intermediate goods perspective.

5 Policy recommendations

The more the UK reaches an independent favourable trade agreement with China after Brexit, the harder it will be for the UK to strike a good deal with EU.

A China-UK free trade agreement has been extensively discussed since the UK's vote for Brexit. Many supporters of Brexit argue that the UK's regained flexibility to strike trade deals with other partners, and in particular with China given its economic size, will be a key advantage. Our analysis indicates that a China-UK FTA will be neither as easy nor as clearly advantageous as portrayed by Brexit supporters. First, it will be very difficult for the UK to reach an agreement with China without first establishing a new post-Brexit partnership with the EU. Negotiating independent MFN tariffs with other WTO members will be a pre-condition if the UK exits the EU customs union, and this process will require time and effort. Second, even if the UK reaches an agreement with China, the UK cannot serve as a back door for Chinese products to enter the EU, because the EU is very likely use rules of origin to close any such loopholes. In addition, entering the EU via the UK will entail an additional transportation cost that will, at least partly, offset any tariff savings, making use of such a loophole less worthwhile. Third, the UK and the other EU economies differ in most of their imports and exports, so there would be very limited substitution between them. Even for the product categories in which the UK and the EU compete on the Chinese market, current MFN tariffs are already too low for there to be further sizable reductions. The only exception is the 'motor cars & vehicles' category, in terms of which the UK, Germany and Slovakia do compete on the Chinese market. It is possible that the UK might gain some advantage were a UK-China trade deal to be signed. However, the cost for the UK might be high, because such a deal could end up creating obstacles for the UK's current most important trade partnership, namely the one it has with the EU.

It therefore seems to us that establishing a new trade relationship with the EU would be a more urgent task for the UK in the post-Brexit world, than an FTA with China. Under such circumstances, the UK might need to postpone its trade negotiations with other economies outside of EU, including China. This goes beyond the current discussion of the illegality of the UK starting to negotiate trade deals before it leaves the EU. The issue is whether it makes economic sense for the UK to do so, and the answer is no. In fact, the more the UK reaches an independent favourable trade agreement with China after Brexit, the harder it will be for the UK to strike a good deal with EU. In the meantime, it is also urgent for the UK to negotiate with the main WTO members on MFN tariffs, because outside the EU, the UK might not participate in the EU schedule of concessions. The best strategy for the UK would be to negotiate with the other WTO members with the EU-based tariffs as a starting point, to avoid negotiating over terms separately and aalso to maintain a close relationship with the EU.

In general, the EU should not be too concerned by a potential China-UK FTA. After all, the overall EU-China trade pattern differs from the UK-China trade pattern. Even if the UK can maintain its EU single market status to the EU, as long as the EU includes rules of origin in its trade negotiations with the UK, there would be at most a limited substitution effect in certain sectors, such as motor vehicles, and this would mainly affect Germany and Slovakia. The overall impact would be very moderate. Therefore, when establishing the new trade relationship with the UK, the EU does not need to overplay the significance of the China-UK factor, and can focus more on its internal priorities.

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