Economics Internal Assessment 3

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Article 3

Milling sector warns of Brexit inflating price of flour[1]

Loaf of bread may rise by 10 cent and Irish bakers may seek alternative to UK suppliers

Mon, Mar 20, 2017, 01:00

With tariffs, the rate the EU charges may add eight to 10 cent to a loaf of bread in the Republic. Photograph: Frank Miller

Brexit could put an extra 10 cent on the price of a loaf in Ireland, the milling industry warned.

Eighty per cent of the flour used in the Republic for baked goods and other products comes from the UK, and may face a significant tariff if a trade deal is not struck between Britain and the EU.

If Irish producers switched suppliers to those operating within the EU to avoid trade barriers, then jobs would be lost in the UK, according to the National Association of British and Irish Millers.

[1] "Milling Sector Warns Of Brexit Inflating Price Of Flour". *The Irish Times*, 2017, http://www.irishtimes.com/business/agribusiness-and-food/milling-sector-warns-of-brexit-inflating-price-of-flour-1.3016495.

Director Alex Waugh said: “If tariffs were to be introduced, the rate the EU normally charges would add eight to 10 cent to a loaf of bread in the Republic.

“It is pretty inflationary, assuming the flour continues to come from the same source as now.”

“Once you introduce a tariff everything changes, so the likelihood is that the flour currently coming from the UK would come from somewhere else in the EU where there would not be a tariff.”

He said the result would be jobs lost in the UK.

Refining flour

Flour is sent from the UK to Ireland to be refined into anything from bread and cakes to coating for chicken nuggets and battered fish.

It is often exported back to the UK as part of finished goods.

Over the last 20 years, the UK has become the main supplier of milled flour to the Republic. The only mill in the Republic is at Portarlington in Co Laois.

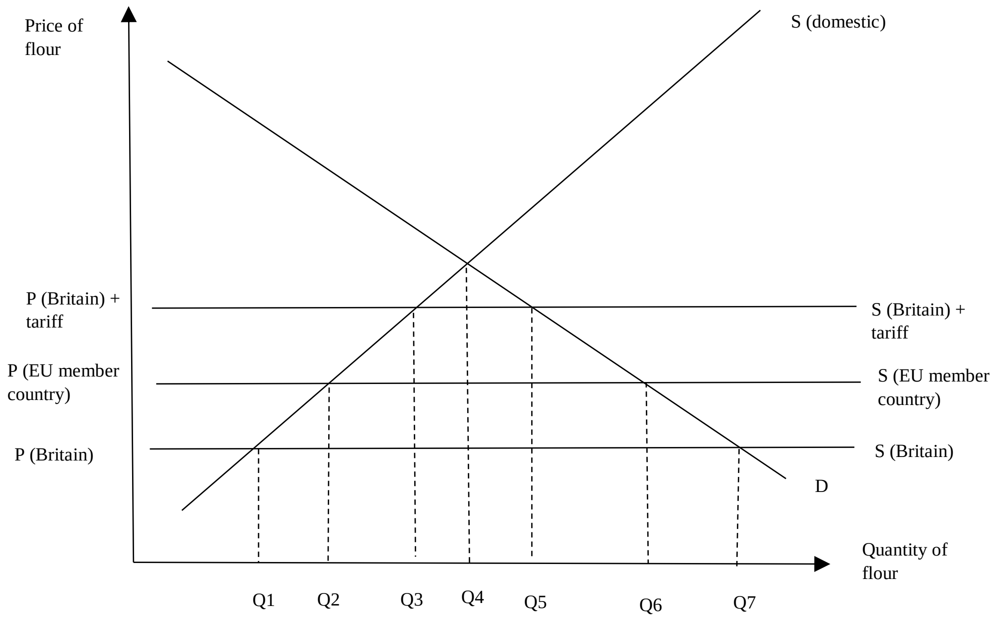
Half of the flour used by Irish bakers is milled on the island of Ireland, a significant proportion of that from Belfast, and the rest comes from England, Mr Waugh said.

He added: “What we are seeing is politicians trying to respond to different pressures in different places. From the point of view of our business, maintaining that tariff-free trade between the UK and Ireland is crucial.” – (PA)

Commentary 3

This extract illustrates the flour market in the Republic of Ireland (who will remain as part of EU after Brexit as it is separated from Northern Ireland who is part of United Kingdom) and explores possible effects of the tariff (is a tax levied on imports to reduce the level of imports in a country) as a result of Brexit (Britain leaving the European Union). The European Union (EU) is a customs union, where its member countries enjoy free entry and exit at all the member borders. It also implies that there are lower trade barriers for member countries and higher trade barriers for non-members. The Republic of Ireland and Britain were originally part of the EU. Britain leaving the EU would mean that Britain will not enjoy the free trade privileges with the EU anymore. Instead, the EU will impose higher trade barriers on Britain, which is why there is going to be a tariff (a tariff is a duty to be paid for imports to restrict trade) on British flour. The effects of the tariff on the flour marker in the Republic of Ireland will be illustrated by Figure 1.

Figure 1: Effects of tariff on British flour in Republic of Ireland

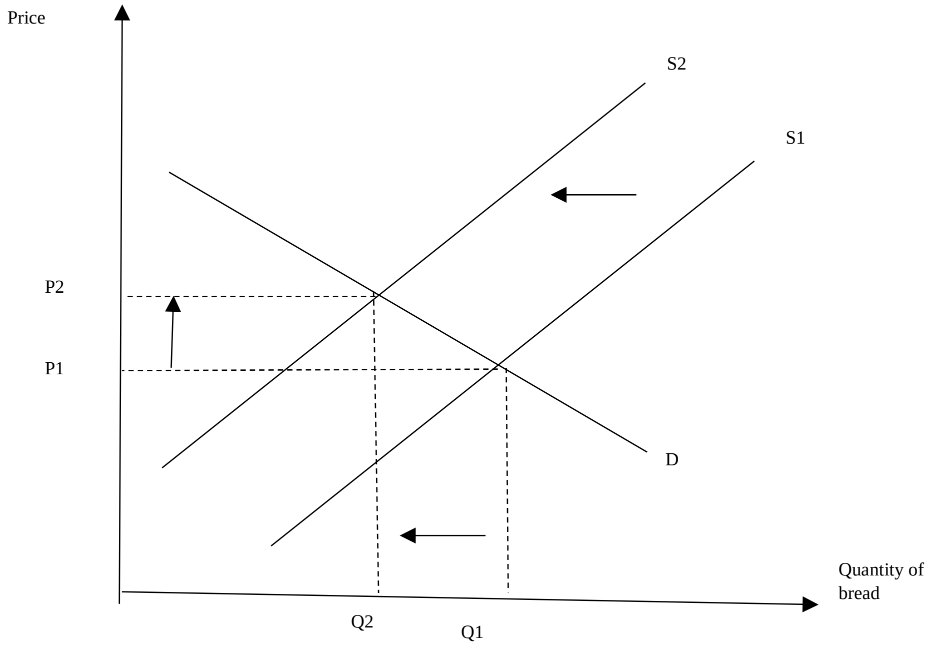


Initially, without any tariff imposed, the price of flour is at P(Britain). Ireland will consume 0Q7 of flour and import Q1-Q7 from Britain. With the "significant tariff" imposed on British flour, the price of flour from Britain will increase to P(Britain) + Tariff, reducing consumption to 0Q5 and imports to Q3-Q5. However, it is likely that after the tariff is introduced, Irish flour consumers will switch to buying flour from other EU member “where a tariff is not imposed” at P(EU) and hence cheaper than flour from Britain. The lower price leads to more consumption to 0Q6, of which Q2-Q6 is imported from other EU members. This will increase the revenue of Irish flour producers as their production will increase from Q1 to Q2. Overall, the price of flour in the Irish market will increase and consumption of flour and consumer choice will decrease as a result. In addition, there will be a loss of world efficiency as Q1-Q2 will be produced by the less efficient Irish producers.

However, since no tariff will be levied on other EU member countries, “the flour currently coming from the UK would come from somewhere else in the EU”. The tariff will cause unemployment in the British flour industry as Britain will lose Q1-Q7 worth of export revenue from selling flour to Ireland.

The increase in price of flour in the Irish market will raise the price of the loaf. This is because flour is a raw material for making bread, therefore the tariff will increase cost of production of final goods and increase the price of bread in Ireland. This is illustrated in Figure 2.

Figure 2: Bread market in Ireland



According to the article, this tariff will cause each loaf to be increased by 10 cents due to the increase in price of flour, regardless whether the producers continue using British flour or buy flour produced by other EU members. This shows that the tariff will ultimately hurt the Irish consumers because of the higher prices that they will have to pay for a necessity like bread. The higher prices will ultimately hurt the lower income group in Ireland most. Note that flour is the raw material for a lot of other finished goods in the food industry and the tariff may lead to cost-push inflation (the general increase of prices and fall in the purchasing power) in the Irish market.

The effects of the tariff are obviously disadvantageous to both countries, especially those in the lower socio-economic class. The increase of price of flour in the Irish market will lead to increased prices for Irish consumers and could also lead to inflation, while in Britain there would be a significant loss of jobs and increased unemployment in the flour industry. In the short run, there could be a sharp spike in prices of bread as producers try to find alternative flour suppliers within the EU. However in the long run, prices of bread should stabilise but local flour industries may become more inefficient due to the protection given by the tariff. In order to minimise these negative effects, Britain and the Republic of Ireland need to make deals to reduce the avoidable negative impacts from the impending tariff on British goods imposed by the EU. However this is unlikely as Brexit has caused huge strain on the relationship between Britain and the Republic of Ireland.