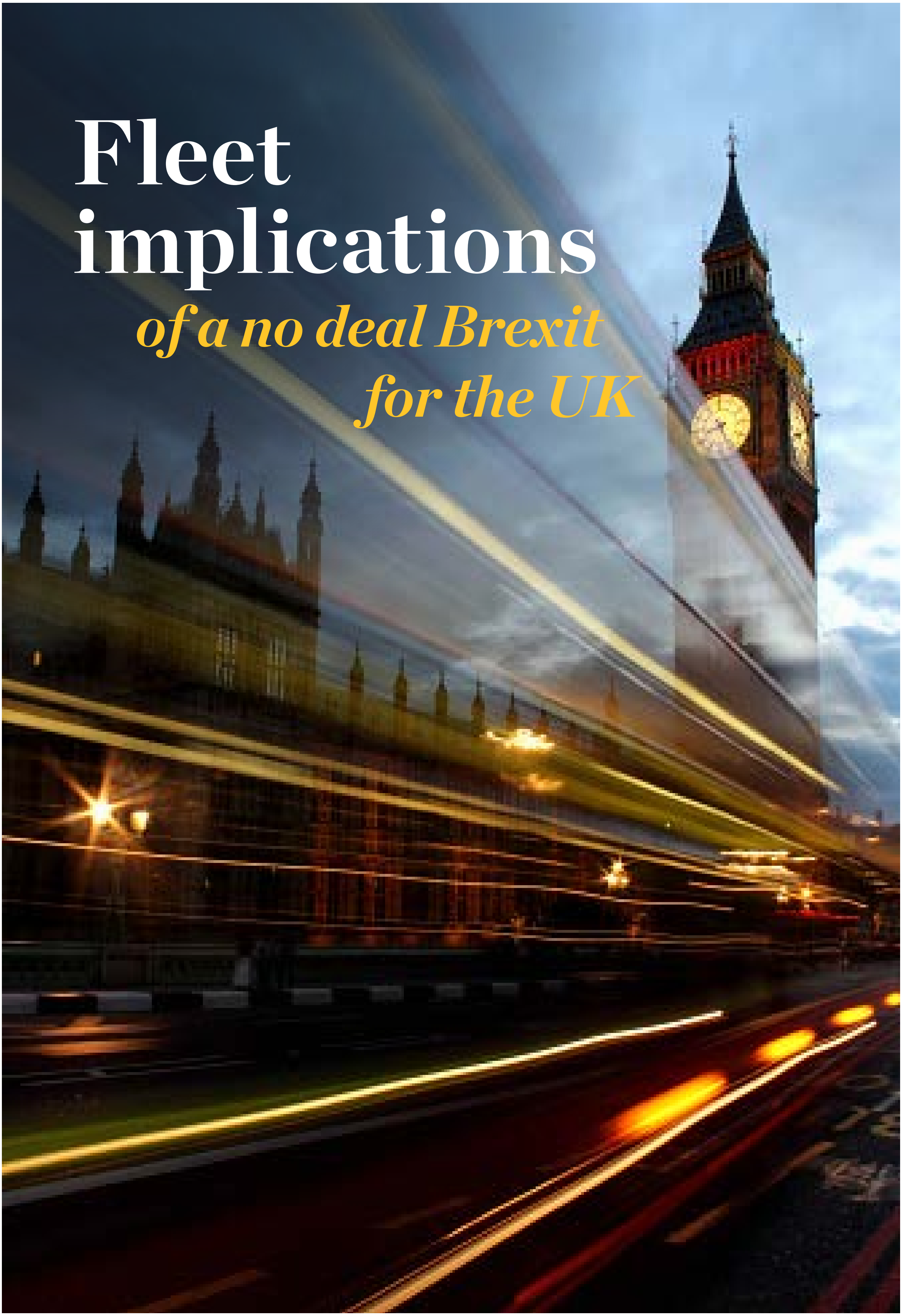
Fleet implications

of a no deal Brexit for the UK



Venson fleet management solutions

Company vehicles are an important asset for supporting core business operations and that's why our contract hire and fleet management solutions are created in response to our clients' needs and are based on our commitment to long term partnership and exceptional customer service.

Testimony to this is our customer retention rate of over 95%. Along with exceptional service we ensure our clients receive great value from their fleet, by delivering solutions that are based on impartial advice and that provide tangible financial return. We can do this because we've only ever specialised in managing fleets, so our knowledge and in-depth understanding of the market is the best in this sector and relevant to public, private, not for profit and emergency service organisations. We also believe in true partnership, working with fleet operators and their drivers to ensure they always receive the most appropriate solution to support their organisation's operational and financial needs.

venson

Executive SUMMARY

The UK's withdrawal from the European Union – Brexit – has been called "the greatest challenge of our times" by the Society of Motor Manufacturers and Traders.

While the British Vehicle Rental and Leasing Association (BVRLA) says that Brexit is the "number one priority" amongst its members, which include Venson Automotive Solutions.

Both fear the UK leaving the European Union on March 29, 2019 with no trade deal in place with the result being that World Trade Organisation (WTO) tariffs are introduced.

That will trigger price increases – unless brands and their retail networks can absorb the additional costs which some have already warned they cannot – with the bold figures being: the list price of cars rising by 10%; commercial vehicle prices rising by up to 22% (an average 13.5% for light vans); and the cost of vehicle components by up to 4.5%.

What's more, some motor manufacturers have warned that the burden of price rises could mean that available model choice is reduced.

Meanwhile, fleets can expect the in-life cost of vehicle operations to also rise as a result of a 'no-deal' Brexit. Experts have suggested that service, maintenance and repair (SMR) costs could rise by 10%, while such an increase – along with the rise in the price of components – would also trigger a surge in insurance premiums.

Besides potential vehicle and component price increases, a 'no-deal' Brexit could mean that fleet operations are impacted by the imposition of non-tariff barriers with the result that the delivery of new vehicles and replacement parts far from being 'just in time' are delayed due to customs changes and a raft of other red tape.

Further adding to the complexity is the devaluation of Sterling, which if it continues to fall would potentially result in further price rises across the whole fleet supply chain in addition to those resulting from the imposition of WTO tariffs.

The UK automotive industry believes that the complexity of negotiating a new trading relationship with the European Union means that such an agreement cannot be in place by March 2019.

As a result, it is calling for agreed 'interim arrangements' or 'transitional arrangements' to be in place to avoid the so-called 'cliff-edge' of enforced WTO trading rules immediately coming into play, which the SMMT, called: "**The worst foreseeable outcome for the sector, its employees and the British economy.**"

Against the background of on-going diplomacy and economic uncertainty, new car and van registrations are falling as are the number of new vehicles rolling off production lines in UK factories – with Brexit an influencing factor on both.

However, with all challenges there are opportunities and fleet chiefs must assess the impact of a 'no-deal' Brexit, generate options and be prepared.

March 29, 2019 is a long way off and the reality is that Brexit negotiations are likely to be protracted and could continue much longer than the government's two-year forecast in terms of having new trade agreements in place.

So fleets must continue to operate against a background of what is known and manage their assets effectively and efficiently. That means continuing to evolve because standing still awaiting the outcome of Brexit, which will take many months and even years, simply means costs will escalate.

As ever, negativity and uncertainty creates a fear-factor and that slows decision-making. However, given the slowdown in new vehicle registrations already seen in 2017 and the trend expected to continue in 2018, fleets prepared to invest in new cars and vans may reap financial rewards.

This report analyses what impact the UK leaving the European Union without a trade deal could have on fleets and the wider motor industry; the background to those changes and the fears that exist; but concludes with advice for fleet decision-makers on how they might transform their vehicle operations over the coming months.

Venson is in discussions with all the major motor manufacturers and working to provide customers with a number of different scenarios/options to safeguard as far as possible against Brexit-inspired cost increases in respect of both vehicle acquisition and in-life operation.

One option, for example, might be to implement a post-Brexit 'no-deal' plan that may potentially see fleets composed of a greater percentage of cars and vans manufactured outside of the European Union.

That's because vehicles sourced from outside of the European Union may be more insulated against price rises. However, in a global industry 'Rules of Origin' will determine the 'made in' location of origin and not the country where a manufacturer is headquartered.

Brexit

and the UK's withdrawal from the European Union

Following the UK referendum vote on June 23, 2016 to leave the European Union, the government and the European Union have been conducting negotiations on withdrawal – known as Brexit.

A key feature of those negotiations is the UK's future trading relationship with the European Union. The UK's membership of the Single Market has enabled the automotive sector to trade freely with the European Union without incurring the cost of tariff and non-tariff barriers. As a result, the motor industry is united in aiming to secure tariff-free access to European and other global markets.

The Society of Motor Manufacturers and Traders (SMMT) says one of its Brexit priorities is: **"Unrestricted access to the single market of Europe, our largest trading partner. This is essential not just for the import and export of vehicles but also for the trade of components, essential for the production of vehicles and other automotive products in the UK."**

It adds: **"The government must demonstrate how it intends to secure a future trade agreement with the European Union that affords the automotive industry the benefits currently enjoyed as members of the Single Market. Under a new customs agreement with the European Union, government should prioritise the free-flow of automotive goods at the border to avoid costs, maintain competitiveness and support the just-in-time manufacturing process."**

The UK government has published white papers on the Customs Bill and trade. The Customs Bill white paper sets out plans to legislate for the UK's post-Brexit, standalone customs, VAT and excise regimes. The trade white paper explores options for an independent UK trade policy after Brexit. The government is seeking views in response to both of those papers and the SMMT is co-ordinating an industry response.

The SMMT has met with Prime Minister Theresa May, a wide range of ministers and MPs and the members of the House of Lords to discuss Brexit and the impact on the automotive sector. In addition, meetings have been held in Brussels with the European Commission, as well as European automotive industry trade bodies.

The government said in its 'Industrial Strategy' white paper, which was published in November 2017: **"The decision to leave the European Union was not a decision to retreat from the world. In fact we need to embrace it. There are opportunities to be gained from leaving the European Union. Britain's future has to be one of free trade with the whole world, including with the rest of Europe.**

"The government believes it is overwhelmingly in our mutual interest to agree a comprehensive and ambitious UK-European Union economic partnership that enables the most free and frictionless trade possible with minimal disruption to business."

Additionally, the government is in discussions with a number of countries about future options, including full free trade agreements.

However, the government does acknowledge the existence of uncertainty while the "precise nature" of the UK's trading arrangement with the European Union is discussed.

The 'Industrial Strategy' white paper added: **"To minimise this, we are seeking to agree an implementation period, of around two years, to allow businesses to adapt to the new arrangements."**

The media regularly highlights organisations calling for an "implementation period" and a "transition period" as though, in relation to Brexit, they are one and the same. However, as William Wright, managing director of capital markets think tank New Financial, wrote in The Daily Telegraph (November 27, 2017): **"The key difference is timing. An 'implementation period' would first require reaching a trade deal with the European Union to implement and is based on what many people think is an optimistic assumption that the UK can negotiate such a deal by March 2019. A 'transition period' would need to be agreed before a trade deal is reached. It explicitly accepts that the chances of clinching a deal in the next 17 months are slim, and is in effect an extension to the negotiation process. It would mean that regulation and market access would remain unchanged for a few years after Brexit, giving politicians more time to negotiate a better deal."**

SMMT president Tony Walker speaking at the organisation's 101st Annual Dinner in London 24 hours after publication of the government's 'Industrial Strategy' white paper called for faster, concrete progress in agreeing a Brexit transition period to avoid a 'cliff-edge'. Additionally, he urged the government not to undermine the UK automotive industry's hard won competitiveness due to slow progress on Brexit.

He said there was no substitute for free and frictionless trade, and called for quicker progress on agreeing a transition period following Brexit.

The transition, he added **"should be on the current terms and, crucially, not time-limited"** to give industry time to adjust and secure long-term investment decisions.

He continued: **"We will never stop striving to be competitive. But we ask government to help provide the conditions in which we can compete. Like every other industry, we need certainty now.**

"After all the difficulties we have overcome, all the changes we have made and the innovations we have brought, we do not need trade barriers to be our next challenge. We are an industry with the character to overcome major obstacles. And we are working hard to maintain our competitiveness. But don't test our character unnecessarily."

He added: **"In the last 40 years we have succeeded. We have torn down so many barriers. Please don't allow new ones to be erected."**

But, against the background of diplomacy, new car and van registrations are falling as are the number of new vehicles rolling off production lines in UK factories – with Brexit an influencing factor on both.

UK new car market registrations were down almost 5% in 2017 versus 2016's record total. SMMT chief executive Mike Hawes said: **"Declining business and consumer confidence is undoubtedly affecting demand in the new car market."**

Registrations of light commercial vehicles under 3.5 tonnes were down almost 4% in 2017 compared with 2016's record high, with Mr Hawes saying: **"The recent decline in business confidence, caused by economic and political uncertainty, is now having an impact. Government must therefore address these concerns and create the conditions necessary for the market to prosper."**

The latest manufacturing figures published by the SMMT showed that UK car production was also falling, down 1.6% in 2017 versus 2016, while van production was down 13.3% year-on-year.

Mr Hawes said: **"Brexit is the greatest challenge of our times and yet we still don't have any clarity on what our future relationship with our biggest trading partner will look like, nor detail of the transitional deal being sought. Leaving the European Union with 'no-deal' would be the worst outcome for our sector so we urge government to deliver on its commitments and safeguard the competitiveness of the industry."**

A 'no-deal' – or a so-called 'hard Brexit' – on the UK's future trading relationship with the European Union is "not an option" because it would lead to the imposition of WTO tariffs (see below).

The SMMT fears that such tariffs would make UK vehicle exports uncompetitive in European Union member States and thus trigger a dramatic downturn in manufacturing levels with factories potentially closing and huge jobs losses across the automotive supply chain.

European Union chief Brexit negotiator Michael Barnier said in a speech in November 2017 that the 27 remaining member States would be ready to offer the UK the "most ambitious" free trade agreement approach.

He continued: **"The UK will, of course, have access to the Single Market. But this is different from being part of the Single Market. And a good deal on our future relationship should facilitate this access as much as possible. And avoid a situation where trade would happen under the WTO rules for goods and services.**

"For the first time ever in trade talks, the challenge will be to limit divergence of rules rather than maximise convergence.

"If we manage to negotiate an orderly withdrawal, fully respect the integrity of the Single Market, and establish a level playing field, there is every reason for our future partnership to be ambitious. This is our preferred option."

Mr Barnier's Task Force 50 is responsible for negotiating transport, the Single Market and customs' Brexit rules and it is the intention to conclude negotiations by October 2018 to provide enough time for ratification of the withdrawal agreement on a range of key issues.

At that point the Task Force is hoping to be able to agree the scope of the new relationship with the UK, although, it says, details of a trade agreement – and new customs procedures – would likely be agreed later.

The European Union says that whether a trade deal can be agreed, there will be frictions and customs controls no matter what, come 'Brexit day'.

As a result, trade facilitation measures will not remove all frictions and the European Union adds: **"There is also a risk that the trade deal, which will only be agreed and ratified post-Brexit, might require unanimous approval from all 27 member states, which could lengthen the ratification process."**

Similarly, WTO rules mean that the UK government would impose potentially similar levels of tariffs on cars, light commercial vehicles and components imported into the UK from European Union member States. That would mean significant price rises for fleets and consumers.

If at the end of the negotiating period there is agreement on a future relationship, current arrangements should continue to apply, including maintaining membership of the Single Market and Customs Union to ensure continuity and certainty, according to the SMMT.

"We need unrestricted access to the Single Market of Europe, our largest trading partner. This is essential not just for the import and export of vehicles but also for the trade of components essential for the production of vehicles and other automotive products in the UK," says the SMMT.

However, the UK automotive industry believes that the complexity of negotiating a new relationship with the European Union means that such an agreement cannot be in place by March 2019.

As a result, it is calling for agreed 'interim arrangements' or 'transitional arrangements' to be in place to avoid the so-called 'cliff-edge' of enforced WTO trading rules coming into play on March 29, 2019 which, the SMMT, called: **"The worst foreseeable outcome for the sector, its employees and the British economy."**

In the longer term, the SMMT says that government must ensure that the UK's new trading terms with the European Union and the rest of the world are **"as good as or better than those already enjoyed by the automotive sector".**

Key Fact 1

SMMT: **"Brexit is the greatest challenge of our times. 'no-deal' is not an option."**

Key Fact 2

Two key tariff priorities:

- **Establishing a permanent deal which ensures that the UK automotive industry is able to sell into the European Union free of tariffs.**
- **As part of negotiations ensuring that transitional measures are put in place (if required) to prevent tariffs being placed on UK automotive exports during any gap between the UK leaving the European Union and establishing a new trading relationship.**

Source: SMMT

The UK automotive industry believes that the complexity of negotiating a new relationship with the European Union means that such an agreement cannot be in place by March 2019.

The World Trade Organisation (WTO) is the only global international organisation dealing with the rules of trade between nations.

World Trade Organisation *tariffs explained*

At its heart are the WTO agreements, negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments – there are 164 members of the WTO. The goal is to ensure that trade flows as smoothly, predictably and freely as possible.

WTO agreements provide the legal ground rules for international commerce. They are essentially contracts, binding governments to keep their trade policies within agreed limits.

Although negotiated and signed by governments, the goal is to help producers of goods and services, exporters, and importers conduct their business, while allowing governments to meet social and environmental objectives.

The system's overriding purpose is to help trade flow as freely as possible – so long as there are no undesirable side effects – because that is important for economic development and well-being.

The WTO agreements cover goods, services and intellectual property. They spell out the principles of liberalisation, and the permitted exceptions. They include individual countries' commitments to lower customs tariffs and other trade barriers, and to open and keep open services markets.

Customs duties on merchandise imports are called tariffs. Tariffs give a price advantage to locally-produced goods over similar goods which are imported, and they raise revenues for governments.

Non-tariff barriers restrict imports and exports of goods and service through mechanisms other than the imposition tariffs. Such obstacles, in addition to 'Rules of Origin' (see below), may include: Import licensing and/or quotas, subsidies, rules for valuation of goods at customs, customs delays and pre-shipment inspections and other red tape and fees on goods that currently move friction-free across borders.

Agreements are not static; they are renegotiated from time to time and new agreements can be added to the package.

About half of the UK's trade is already on WTO terms – with the United States, China and a number of major emerging nations where the European Union does not have trade agreements. For example, the European Union does not have trade deals with Brazil and India.

As a result, according to Roberto Azevedo, WTO director general quoted in The Sunday Telegraph (November 26, 2017): **"It's not the end of the world if the UK trades under WTO rules with the European Union."**

While acknowledging that a free trade agreement would be best, with WTO rules involving reciprocal UK-European Union tariffs, Mr Azevedo said: **"If you don't have a fully functioning free trade agreement with the European Union, there could be rigidities and costs – but it's not like trade between the UK and European Union is going to stop. There will be an impact, but I suppose it is perfectly manageable."**

What's more, giving support to optimists who believe that Brexit will be good for the UK, he added that the nation could be "more flexible in its approach and quicker to react within the WTO, as you don't have to coordinate with all the other members of the European Union".

Mr Azevedo concluded: **"I think Britain has an opportunity. A chance to contribute in a way that is consistent with the quality of your professionals and the size and importance of your economy."**

The European Union has been a WTO member since January 1, 1995 and is a single Customs Union with a single trade policy and tariff. However, the 28 member States of the European Union are also WTO members in their own right. Nevertheless, the European Commission – the EU's executive arm – speaks for all European Union member States at almost all WTO meetings.

As mentioned above different products are subject to different levels of tariffs. The European Union tariff on cars imported into the UK and other member States from non-member countries is 10%; tariffs on commercial vehicles are up to 22% with an average of 13.5% for light vans; and tariffs on components up to 4.5%.

By comparison, import tariffs imposed by other major automotive manufacturing countries outside the European Union are respectively: Japan – no tariffs; South Korea – 8% on cars; 10% on light commercial vehicles; and 8% on components; United States of America – 2.5% on cars; 25% on light commercial vehicles; and 2.5% on components.

However, with some countries, such as Canada, South Africa and South Korea, the European Union has negotiated free trade agreements (FTAs), which means tariffs are not imposed. In total there are 67 FTAs between the European Union and other countries.

Wilbur Ross, the United States Commerce Secretary and one of President Donald Trump's most senior advisers, speaking at November 2017's Confederation of British Industry (CBI) conference gave an insight into the different demands of trading partners.

A total of 14.5% of UK manufactured cars are exported to the United States of America and Mr Ross highlighted that the European Union imposed higher tariffs on most imported goods specifically pointing out that it was 10% on cars, compared with the United States of America's 2.5%. The obvious implication being that the European Union favoured protectionism.

Nevertheless, he concluded that **"assuming there are no big landmines in the UK's exit agreement from the European Union"** a new UK-United States of America trade deal **"shouldn't take terribly long".**

Key Fact 3

A 'cliff-edge' 'no-deal' Brexit would see tariffs imposed resulting in price rises:

- **Cars 10%**
- **Commercial vehicles up to 22% (average 13.5% for light vans)**
- **Vehicle components up to 4.5%.**

RULES OF *origin*

A critical issue for the automotive industry is 'Rules of Origin', which determine the source of goods.

'Rules of Origin', which explain the 'made in' label applied to products, are the criteria needed to determine the economic nationality of a product for the purposes of international trade and subsequently the trade rules, including tariffs, that should apply when importing or exporting.

But automotive manufacturing is a highly complex industry so determining the 'Rules of Origin' is far from simple.

For example, a single vehicle part may be composed of more than 30 components, and undergo more than 100 process steps to become a finished product, according to the European Automobile Manufacturers' Association (ACEA). It may pass through 15 countries, and cross borders multiple times in its material journey. A single vehicle, in turn, consists of around 30,000 parts.

Vehicle manufacturers currently operate some 300 assembly and production plants in Europe. They often manufacture engines or transmissions in one country and assemble the final vehicle in another. The European Single Market provides for a high level of economic and regulatory integration in that respect. Consequently, the level of integration is reflected in how the automotive industry has strategically set up its business operations in terms of supply chains, production sites and distribution networks.

Erik Jonnaert, ACEA secretary general, said: **"Today, the automotive industries of the European Union and the UK are closely integrated; from the economic, regulatory and technical points of view. Any changes to this level of integration will most certainly have an adverse impact on automobile manufacturers with operations in the European Union or the UK, as well as on the European economy in general."**

However, there is no globally accepted template to determine whether a product originates from a particular country. Each country can apply its own rules of origin scheme which creates the problem of differing standards of proof for products being imported and exported between differing countries.

Nevertheless, the two most common bases upon which countries determine whether a product has originated in a particular country are: Where the goods are 'wholly obtained'; and the location where the 'last, substantial transformation' took place.

There are two common types of 'Rules of Origin', 'preferential' and 'non-preferential'. 'Preferential Rules of Origin' only apply where there is a specific preferential trading arrangement in place, for example a FTA or a Customs Union. It follows, therefore, that 'non-preferential Rules of Origin' can be used for the purpose of determining quotas, anti-dumping and anti-circumvention measures, statistical analysis and origin labelling.

As the UK is a member of the European Union Customs Union, 'Rules of Origin' do not need to be considered when exporting or importing from the rest of the European Union. Similarly trading outside of the European Union, goods carry a 'made in the European Union' sticker and given the volume of components sourced from member states have 'originating status'.

However, following Brexit, depending on the nature of the UK's new trading relationship with the European Union, new 'Rules of Origin' will potentially have to be developed to identify goods that have come to the UK from the European Union and vice versa.

The SMMT hopes that with regards to trade with the European Union, the UK could "expect 'Rules of Origin' to be agreed so as to facilitate the application of tariff concessions".

Currently, British businesses seeking to comply with 'Rules of Origin' set in existing FTAs have to take a number of steps to provide proof that goods originate in the UK.

Existing European Union FTAs require approximately 50% European Union content if a finished vehicle is to benefit from the preferential terms of trade with a third country.

However, if new trade deals signed by the UK were to require 50% domestic content in a finished vehicle, a significant change in the supply chain would be needed, according to the SMMT.

Vehicles produced in the UK currently contain approximately 41% UK content – growth in recent years but still a long way from the 50% that would potentially be required to enjoy preferential treatment under future trade deals.

With regards to trading with countries outside the European Union, the SMMT says: **"Should the UK secure continuing access to the preferential trading terms of already agreed European Union FTAs, it should follow that existing 'Rules of Origin' remain in place.**

"However, should the UK not secure such access or choose to negotiate new free trade agreements with third countries, it will have to negotiate new 'Rules of Origin'."

It is estimated that only 25% of a car manufactured in the UK can be considered as 'originating' under global trade rules.

Therefore, irrespective of how generous the terms of any FTA might be, the need to comply with 'Rules of Origin' processes will result in significant new administrative costs as motor manufacturers – and their component suppliers – will need to generate and supply paperwork to demonstrate the origin of goods. That significant burden will translate into additional administration costs that could be expected to result in the price of vehicles increasing.

Key Fact 4

Vehicles produced in the UK currently contain approximately 41% UK content – a growth in UK content in recent years but still a long way from the 50% that would potentially be required to enjoy preferential treatment under future trade deals.

UK automotive trade with the European Union

and the rest of the world

Unless access to the Single Market can be negotiated following the UK's withdrawal from the European Union, tariffs will be imposed on imports and exports to and from the remaining member States.

Key Fact 5

The vast majority of cars sold in the UK are imported from European Union member States.

What's more, as a member of the European Union, the UK has access to preferential trading terms with 74 third countries and territories such as the recently ratified European Union trade deal with Canada. The UK is also party to seven open negotiations, including those with the United States of America and Japan.

Therefore, the UK's European Union withdrawal brings into questions its access to trade agreements already signed by the European Union, as well as those that are currently being negotiated.

More than 80% of cars sold in the UK are imported from European Union member States, according to ACEA, although the SMMT quotes a lower figure (69%). Germany is by far the largest exporter to the UK, followed by Belgium, Spain and France. Separately, PA Consulting Group, a consulting, technology and innovation firm, calculates that in 2016 a total of 2.4 million vehicles were exported from the European Union to the UK.

UK exports to European Union countries currently account for 56% of domestic car production with the largest markets being: Germany (8.6%), Italy (7.2%), France (6.7%) and Belgium (6.2%). The UK currently exports cars to more than 160 countries worldwide. The United States of America (14.5%), China (6.5%), Turkey (3.1%), Australia (2.5%), Japan (1.9%), Canada (1.8%) and South Korea (1.7%) are the largest non-European Union export destinations for the automotive sector.

While it is likely that the UK will look to negotiate new trade deals with key markets across the globe, it is unlikely, both for reasons of legality and administrative capacity, that any new deals would be agreed before UK withdrawal from the European Union takes place.

The average bilateral trade deal takes more than three-and-a-half-years to be implemented so it could take many years before new arrangements with key trading partners are in place.

There was also a genuine risk, according to the SMMT, that the UK would be unable to secure trading terms that were equally as beneficial as those already negotiated by the European Union.

Therefore, the UK's withdrawal from the European Union could result in a number of unwelcome outcomes in relation to international trade, including, says the SMMT:

- **New costs and barriers to trade with third countries as a result of a loss of access to European Union trade agreements; and**
- **A competitive disadvantage as a result of not having access to European Union trade agreements currently under negotiation.**

The nightmare scenario for the UK automotive industry is, according to the SMMT that: **"The application of tariffs would put the UK automotive industry for both vehicles and parts at an immediate competitive disadvantage, which could ultimately make automotive manufacturing in the UK unviable."**

Forecast impact of tariffs

on UK new car and light commercial vehicle prices

The UK automotive sector currently has tariff free access to the European Single Market.

That means the UK can trade with the other 27 member States in terms of imports and exports without the imposition of tariffs.

However, following Brexit, unless the UK's access to the Single Market can be negotiated, WTO import and export tariffs to and from those member States will apply and the knock on impact is likely to be significant price rises.

About 85% of cars – around 2.3 million – bought in the UK are imported, the majority of which – up to 87% – currently come from the European Union, according to the National Franchised Dealers Association (NFDA). It says that in total, 95% of cars imported to the UK do not currently face a tariff as they come from the European Union, or from countries which have free trade agreements with the European Union.

In terms of the automotive industry the tariffs that can be expected to apply on imports to the UK from remaining European Union member States, as previously explained, are:

- **Cars 10%**
- **Commercial vehicles up to 22% (average 13.5% for light vans)**
- **Vehicle components up to 4.5%.**

Similar tariffs can be expected to be applied by the UK government on exports to European Union member States.

The Department for Business, Energy and Industrial Strategy says: **"Tariffs form an important part of the total trading cost to all types of business involved in international trade. However, the government is looking at the costs of trade holistically to understand the full implications to business, the economy and consumers. Ensuring that UK businesses remain competitive and can continue to maximise trade opportunities with European partners and enjoy wider opportunities is a key priority for this government."**

The Department added that to "**minimise disruption and maximise certainty" the government was seeking to agree the detailed arrangements of an implementation period as early as possible and added that it was "proposing that during this period access to each other's markets should continue on current terms".**

The European Union is by far the largest market for the UK automotive sector: more than 80% of cars imported to the UK come from the European Union and 56% of cars produced in the UK are exported to member States.

SMMT analysis suggests that European Union tariffs on cars alone could add at least an annual £2.7 billion to imports and £1.8 billion to exports – a total additional cost of at least £4.5 billion to the UK automotive industry's annual overheads.

As a result, import tariffs alone could push up the list price of cars imported to the UK from the continent by an average of £1,500 if brands and their retail networks were unable to absorb those additional costs, according to SMMT analysis.

The application of tariffs, said the NFDA, which represents the interests of franchised motor retailer, **"would have the potential to raise costs significantly".**

Highlighting that **"tariffs inevitably make cars and parts more expensive"** for fleets and consumers; and manufacturers would divert production to more profitable markets rather than absorb the increased cost of importing to the UK, the NFDA said: **"Retailers, which are already operating on thin margins – a 1% net operating margin is not unusual – will have little option but to pass on some if not all of the tariff burden."**

Cars built in the UK but relying on European Union-imported parts, would also be affected with 59% of components imported, most from the European Union, and due to the increased cost of imported parts the cost of vehicle SMR would also rise.

Honda has already warned that it would be unable to absorb the impact of tariffs should there be no free trade deal.

Honda's Swindon factory is the global hub for the new Civic five-door and the company's UK and European headquarters are located in Bracknell.

Like most vehicle manufacturers, European manufacturing and sales operations are highly integrated, resulting in concerns in many areas including the imposition of import and export tariffs.

In written evidence to the House of Commons' Business, Energy and Industrial Strategy Committee, which is investigating the automotive industry as part of its 'Brexit and the Implications for UK Business' inquiry, Honda said: **"A meaningful transition period is required to allow Honda, and our suppliers, the time needed to adapt systems, processes and resources to the new European Union-UK trading environment.**

Outside of the European Union and Customs Union, with no free trade agreement in place, a 10% tariff would be applied to finished vehicles exported from the UK to the European Union under WTO rules.

“Given our complex operations and integrated supply chain, a transitional arrangement should be based on current arrangements – continued membership of the Single Market and Customs Union – in order to avoid more than one point of change. Given our experience of the level of work required for previous changes to customs regimes, a transitional period should be at least two years.

“For Honda, an optimal future European Union-UK would maintain the benefits of the Customs Union, by delivering tariff-free trade between the UK and the European Union.

“With 35% of exports from our Swindon factory exported to the European Union, and 40% of the components used to build cars at Swindon imported from European Union suppliers, frictionless, tariff-free access to the Single Market and Customs Union is vital to our competitiveness.

“Membership of the Single Market and Customs Union provides Honda with several important benefits, including: tariff free access to the European Market, a frictionless border and regulatory certainty. Additionally, the UK’s membership of the Single Market and Customs Union provides us tariff-free trade with important markets around the world.”

Outside of the European Union and Customs Union, with no free trade agreement in place, a 10% tariff would be applied to finished vehicles exported from the UK to the European Union under WTO rules. Honda also benefits from tariff free access to other markets.

Honda said: **“A 10% tariff would make our vehicles uncompetitive, and would impose costs we cannot afford to absorb.”**

In relation to the import of components, Honda told MPs: **“The average WTO tariff on automotive components is 4.5%. As a significant proportion of component parts for vehicles manufactured at Swindon are imported from outside the UK, if the UK were to impose tariffs at this level, we would see a large increase in production costs.”**

The manufacturer concluded its evidence by saying: **“Honda benefits from free trade agreements between the European Union and trading partners around the world. A transitional period would give the UK time to replicate these agreements, as well as agree a deep and meaningful trading and regulatory relationship with the European Union.”**

Ford, Britain’s biggest seller of company cars and vans, told MPs that the cost of the imposition of tariffs would be “significant”. Highlighting that the SMMT had calculated “an average of £1,500 of duty cost to the list price of every car imported”, Ford said: **“This cost would either increase the cost of a vehicle, or reduce the choice available to the consumer – or possibly both.”**

Perhaps the first evidence of vehicle choice reducing due to Brexit arrived in November 2017 with reports that Renault had put on hold the UK launch of its new Alaskan pick-up due to concerns over the impact of Brexit on the currency exchange rate.

Thierry Plantegenest, global vice-president of sales and marketing for Renault Pro+, was quoted on the website of What Van? (November 9, 2017) as saying that although the brand was targeting the pick-up sector for growth in Europe and Africa, it had to weigh up **“the mix between volume and profitability”** when deciding in which markets to introduce the Alaskan.

Renault had been expected to launch the Alaskan in the UK in the first half of 2018 but was now reconsidering whether to bring the Nissan Navara-based model to the UK market. European sales kicked off in France in September 2017.

Key Fact 6

The list price of UK cars could increase by an average of £1,500 if brands and their retail networks were unable to absorb tariff costs.

Key Fact 7

Ford: **“[The cost of tariffs] would either increase the cost of a vehicle, or reduce the choice available to the consumer, or possibly both.”**

Ford also believes that a transitional arrangement is critically important in order to avoid a ‘cliff-edge’ scenario in April 2019 and told the Committee: **“Retaining tariff-free trade between the UK and European Union is Ford’s number one priority, while [also] benefitting from preferential trading terms with third countries under European Union free trade agreements.”**

Two of the major impacts on trade, said Ford, would be:

- **The import of cars and vans into the UK as the bulk of ‘blue oval’ vehicles sold in the UK were imported from the European Union and Turkey, a member of the Customs Union.**
- **The import of components for engines built in the UK and the import of vehicle repair parts.**

That led the company to conclude: **“Leaving the European Union single market and Customs Union, and reversion to WTO tariffs would place a very significant cost on Ford in Britain and across Europe.”**

Vauxhall manufactures the Astra at its Ellesmere Port plant and the Vivaro van in Luton and told the Committee: **“73% of total UK production is destined for the Single Market making access to this market post-Brexit, in both tariff-free and no non-tariff barrier terms, vital.”**

Reports by PA Consulting Group, which has analysed the cost of the UK moving to a WTO regime – 10% tariff on finished cars and 4.5% tariff on component parts – conclude that manufacturers would find it “especially challenging” given their typically low margins.

PA Consulting’s analysis calculates that the potential cost increase under WTO arrangements could be as much as £2,372 per car – a cost increase of up to £2,090 on the finished car and up to £282 on component parts. Equally, European-based manufacturing companies would face similar costs for exporting to the UK from mainland Europe.

Additionally, the analysis suggested that increased time delays at borders could also impact ‘just-in-time’ supply chains that were currently standard for the automotive industry.

PA Consulting said: **“An additional cost of up to £2,372 may affect carmakers’ profitability per car, eliminating their profit margins. Potentially, a significant proportion of the cost will be transferred to the consumer.”**

It continued: **“Any change in tariffs and regulations will immediately impact the automotive supply chain and make sourcing of assembly parts and distribution of finished vehicles more costly, forcing organisations to rethink their medium to long-term strategies. Although the final position is still unknown, what is without question is that the automotive industry must assess the impact, generate options and be prepared?”**

Tim Lawrence, global head of manufacturing at PA Consulting Group, said: **“Both the European Union and the UK would benefit from keeping free trade and supply chains unaffected because any tariffs would be damaging for both sides based on today’s complex supply chain arrangements.**

“Car makers will have to review their manufacturing and supply chain network and investment decisions and plan for scenarios based on extra tariffs.”

Ultimately, the final sale price of a car, van and component is affected by numerous factors other than the cost of manufacturing the vehicle or component, on which tariffs could be placed.

Nevertheless, it is clear that the imposition of WTO tariffs as a consequence of a ‘no-deal’ Brexit will have a significant impact on the final sale price of vehicles and components.

Forecast impact of tariffs

on vehicle service, maintenance and repair bills and other fleet costs

Post-Brexit tariffs and other trade barriers could add 10% to UK car servicing bills, costing fleets an extra £70 per service, according to a report for the SMMT.

The 'Importance of the Aftermarket to the UK economy 2017' report, commissioned by the SMMT from independent consultancy Frost & Sullivan, reveals that a WTO tariff of up to 4.5% on average on imported car parts would mean an average extra £21 a year cost for replacement components.

In a highly integrated tight margin industry tariff-free access is claimed to be "invaluable" and one of the major reasons why vehicles built in the UK source the majority of their supply chain from either the UK or the European Union.

Outside of the European Union, if an average 4.5% tariff rate on components was assumed, based on KPMG and Automotive Council analysis, in 2014 and 2015, the SMMT estimates that the imposition of tariffs could cost the sector £350-£875 million per year for the import of components, reducing the UK's competitiveness and increasing costs for buyers – but a fraction of the several billion pound tariff cost that that would arise from the import of whole vehicles to the UK.

Meanwhile, quotas, subsidies, customs delays and regulatory barriers could add a further £49 to the cost, resulting in a £2.14 billion rise in the UK's collective car maintenance bills and an average annual cost of £777, up from £707.

Some 80% of replacement car parts fitted to British cars are imported, with almost three-quarters of them sourced from European Union-based suppliers.

It was therefore vital, said the SMMT, that the government sought an interim arrangement to avoid a 'cliff-edge' if a trade deal was not finalised at the end of the Brexit negotiation process.

Mr Hawes said: **"If we don't secure a new trading relationship with the European Union that is free of tariffs and customs checks, [there could be] significant increases to annual car repair bills due to new tariffs and other trade barriers. Government must now prioritise an interim arrangement that maintains single market and Customs Union membership until the right trade deal with the EU is implemented."**

The report found the UK's car servicing and repair sector grew further in 2016, with turnover rising 2.4% to £21.6 billion. That was driven by sustained record numbers of new car registrations and greater reliability, leading to more vehicles remaining on British roads for longer but still requiring regular servicing and maintenance. The increasing level of advanced technology in modern vehicles was also a major influencing factor.

A spin-off impact on a rise in the price of vehicle repairs would be an increase in insurance premiums, the Association of British Insurers (ABI) told MPs.

Saying it would be **"concerned by any increase in the cost of repairing cars or replacing car parts as a result of Brexit"**, the ABI pointed out that any increase in the cost of importing parts required for repairing vehicles would **"also effect the ongoing cost of insuring these vehicles"**.

Any increase would come at a time when repair costs are already accelerating rapidly – up an average 33% over the last four years – in part due to vehicles increasingly being fitted with sophisticated electrical features, used for a range of ADAS (Advanced Driver Assistance Systems) technology.

In addition to the cost of more sophisticated parts and more complex repair methodology, the ABI said that the fall in the value of the Pound against the Euro, particularly since June 2016, was having a significant impact on the costs of the complex supply chain for vehicle parts across the European Union.

"As well as potentially impacting the cost of new vehicles, this affects the costs of replacement parts and therefore of settling insurance claims," the ABI told the House of Commons' Business, Energy and Industrial Strategy Committee.

What's more, without any trade deal or transitional arrangements in place a 'cliff-edge' of March 29, 2019 could have an immediate impact and see the cost of end-of-contract damage charges on fleet vehicles increase.

End-of-contract damage charges remain among the most contentious issues between fleets and vehicle leasing companies.

Some fleets 'accumulate' repairs – particularly perceived cosmetic scratches and dents – during the lifetime of a vehicle rather than having remedial work undertaken during the contract period.

However, amid the uncertainty of Brexit that strategy may well be flawed with fleets potentially being hit with higher than anticipated end-of-contract damage charges due to the forecast increased cost of repairs post March 29, 2019.

That potential development also further throws the spotlight on the importance of fleet decision-makers having in place a robust work-related road safety programme and thus eliminating the potentially higher cost of vehicle repairs as well as insurance premium rises.

One of the long-established spin-off benefits of businesses implementing a work-related road safety programme is reduced insurance premiums due to employees adopting an improved driving style resulting in fewer crashes.

With the ABI warning of insurance premium increases in a 'no-deal' Brexit world and forecasting a higher cost of vehicle repairs, ensuring a comprehensive work-related road safety programme is in place will be critical to minimising any potential cost rises as much as possible.

Key Fact 8

Post-Brexit tariffs and other trade barriers could add 10% to UK car servicing bills.

Key Fact 9

ABI: **A spin-off impact on a rise in the price of vehicle repairs would be an increase in insurance premiums.**

The impact of currency fluctuation on UK vehicle and component prices

The volatility of Sterling as the UK negotiates its exit from the European Union is a major issue for motor manufacturers and component suppliers in the global automotive industry.

The value of Sterling against major currencies like the Euro and the United States Dollar following recent falls is around 15% lower than the long run average.

In simple terms that is both good and bad. Falls in the value of Sterling make UK exports cheaper, but it raises the cost of imports, which ultimately leads to price increases. For example, the UK is BMW's second largest market in Europe so it is already taking a hit on exports to the UK with Sterling depreciation.

Experts are forecasting that Brexit will be one of the factors that could result in Sterling and the Euro reaching parity over the next two years. That would signal an approximate 10-12% fall in the value of Sterling.

Indeed, Lloyds Bank's third annual survey of the UK automotive manufacturing sector – 'Automotive Research Report 2017' – highlighted that the most commonly raised challenge as a direct result of the UK leaving the European Union was the increased cost of goods caused by the devaluation of Sterling. It was a concern to 26% of firms questioned.

That gloomy prognosis is largely based on the UK government failing to achieve success in its negotiations with the European Union. However, if progress is made then Sterling could surge.

Conclusion:

What should fleets do?

In short doing nothing is not an option for fleet decision-makers. The UK's final position post-Brexit may be a long way from being known but, just as PA Consulting said in its reports in relation to motor manufacturers and vehicle component producers, fleet chiefs must assess the impact, generate options and be prepared.

The British Vehicle Rental and Leasing Association (BVRLA) says that Brexit is the "number one priority" amongst its members, which include Venson. Asked to elaborate on members' fears, a BVRLA spokesman added: **"It is more of an amorphous economic fear, with no real detail to get to grips with yet."**

With no details on what the future may look like post-March 29, 2019, the BVRLA says that its main concern, like everyone else's, was the macro-economic picture, as not enough details on what the future may look like had emerged to make any plans other than to speculate on the potential impact of 'no-deal'.

In the run-up to March 29, 2019, the BVRLA says: **"Fleet operators need to get used to operating in a climate of uncertainty."**

Speculating that over the coming months there will continue to be "lots of fervent negotiating, most of it centered around obtaining a workable trade deal that replaces the UK's membership of the Single Market", the BVRLA added: **"We expect the UK government to take a very pragmatic approach in retaining most European Union regulations and directives, but any devaluation of Sterling will put major cost pressures on the fleet supply chain as prices of vehicles, tyres and parts are expected to rise."**

Calling, like the SMMT, for the avoidance of a "cliff-edge exit", the BVRLA has demanded that the UK:

- **Has a barrier-free relationship with the European Union**
- **Remains a member of the European Economic Area, or secures tariff-free access to the Single Market.**

With WTO tariffs forecast to increase the cost of imported and exported vehicles to and from the UK as well as in-life vehicle operating costs, the BVRLA said its key demands were necessary to **"continue the sector's ability to purchase from international vehicle manufacturers without having to pass on additional costs"**.

Besides potential vehicle and component price increases, a 'no-deal' Brexit could mean that fleet operations were impacted by the imposition of non-tariff barriers with the result that the delivery of new vehicles and replacement parts far from being 'just in time' were delayed due to customs changes and a raft of other red tape.

Fleet decision-makers were fearful of the outcome of Brexit, according to the Fleet Industry Advisory Group (FIAG). However, the organisation's chairman, Geoffrey Bray, a fleet industry veteran, calls himself an optimist and believes the UK's departure from the European Union will bring opportunities.

He said: **"Fleet decision-makers must acknowledge the fact that the UK is not an isolated market as far as the automotive industry is concerned. The UK is a small market in a global economy and when the automotive industry is making marketing, including pricing, decisions they are made invariably in a worldwide context.**

"It is a challenging and changing world and Brexit will have an impact, but it will also present major opportunities. Businesses must be nimble and alert – and that includes within the fleet arena – and move forward as opportunities occur.

"March 29, 2019 is when the UK is scheduled to withdraw from the European Union. That date is a long way off and the reality is that Brexit negotiations are likely to be protracted and could continue much longer than the government's two-year forecast in terms of having new trade agreements in place.

"Therefore, fleets must continue to operate against a background of what is known and manage their assets effectively and efficiently. That means continuing to evolve because standing still awaiting the outcome of Brexit, which will take many months and even years, simply means costs will escalate."

Companies, including Venson, featuring in the 2017 survey of the UK's top 50 contract hire and leasing companies, the 'FN50' published by trade title Fleet News, highlighted uncertainty around Brexit and the future trading relationship as one of the biggest challenges for the fleet industry in the coming 12 months.

Respondents reported that businesses were putting investment decisions on hold. However, such a move brings with it a range of problems. Not least that further Sterling devaluation will eventually result in price rises – without the impact of WTO tariffs – and, simultaneously, extending vehicle replacement cycles could trigger higher SMR costs.

With typical replacement cycles averaging almost four years for company cars and five years for vans, according to the 2017 Fleet News 'Fleet200' analysis of 200 of the UK's major fleets, businesses that replace vehicles ahead of the UK officially leaving the European Union may benefit from:

- **Improved vehicle residual values due to fewer vehicles entering the used market in four or five years' time, which for those that lease maybe reflected in improved monthly rental rates**
- **The avoidance of any immediate new vehicle price increases as a result of a "no-deal" Brexit**
- **Possible savings on SMR by replacing vehicles rather than extending operating cycles as costs invariably increase as vehicles age**
- **A boost to corporate image and employee well-being as a result of new vehicle investment.**

As ever, fleet decision-makers are reminiscent of high wire trapeze artists: taking account of all the elements is critical to achieving equilibrium. Nevertheless, where there are challenges there are also opportunities.

Key Fact 10

BVRLA: **"Any devaluation of Sterling will put major cost pressures on the fleet supply chain as prices of vehicles, tyres and parts are expected to rise."**

Key Fact 11

FIAG: **"Fleets must continue to operate against a background of what is known and manage their assets effectively and efficiently."**

FACT *file*

- The UK exports vehicles to more than 160 countries – 56% to the European Union, the UK's biggest trading partner
- More than 50% of all cars and 90% of commercial vehicles built in the UK are bought by European customers
- 1.8 million vehicles (1.7 million cars and 94,000 commercial vehicles) were produced in the UK in 2016
- 1.35 million UK-built vehicles were exported in 2016 (78%)
- 69% of UK car imports are from the European Union
- 79% of UK imported components are from the European Union
- 65% of British-built components are exported to the European Union
- It is estimated that 41% of the content of cars built in the UK is sourced from the UK, with an additional 20-50% sourced from elsewhere in the European Union. Although amongst some automotive companies the proportion is higher
- 2.54 million engines were built in the UK in 2016
- UK automotive industry exported products worth £40.1 billion in 2016 (13% of the UK's total export goods)
- The UK was the world's 13th largest manufacturer of vehicles in 2016 and the fourth largest in the European Union after Germany, Spain and France
- Jaguar Land Rover is the UK's largest vehicle manufacturer followed by: Nissan, BMW (MINI and Rolls-Royce), Toyota and Honda
- The top five models produced in the UK are: Nissan Qashqai, Toyota Auris, Nissan Juke, Land Rover Evoque and Land Rover Discovery Sport
- Vauxhall is the leading commercial vehicle manufacturer in the UK
- There are more than 2,500 automotive component providers in the UK
- There are now no British-owned mass car manufacturers operating in the UK.

Major UK vehicle and engine manufacturing locations

- **Aston Martin, Gaydon** (Comet, DB9, DB11, Rapide, Vantage, Vanquish)
- **Bentley, Crewe** (Bentyaga, Continental, Mulsanne)
- **BMW, Hams Hall** (engine range)
- **Ford, Bridgend and Dagenham** (engine range)
- **Honda, Swindon** (Civic, CR-V and Jazz)
- **Infiniti, Sunderland** (Q30)
- **Jaguar Land Rover, Castle Bromwich, Halewood, Solihull and Wolverhampton** (engine range, F-Pace, F-Type, XE, XJ, XF, Discovery, Discovery Sport, Range Rover, Range Rover Sport and Evoque)
- **MG Motors, Longbridge** (MG3 and MG GS)
- **MINI, Oxford** (3 and 5 door hatch, Convertible, Clubman, Coupe and Roadster)
- **Nissan, Sunderlan**d (engine range, Juke, Leaf, Note and Qashqai)
- **Rolls-Royce, Goodwood** (Ghost, Phantom and Wraith)
- **Toyota, Burnaston** (engine range, Auris and Avensis)
- **Vauxhall, Ellesmere Port and Luton** (Astra five door hatch and Sports Tourer and Vivaro van)

Sources and further information:

British Vehicle Rental and Leasing Association:
https://www.bvrla.co.uk/

Department for Business, Energy and Industrial Strategy – 'Industrial Strategy' white paper:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/662508/industrial-strategy-white-paper.pdf

European Automobile Manufacturers' Association:
http://www.acea.be/

Frost & Sullivan/Society of Motor Manufacturers and Traders – 'The Importance of the Aftermarket to the UK Economy 2017' report:
https://www.smmt.co.uk/wp-content/uploads/sites/2/The-Importance-of-the-UK-Aftermarket.pdf

House of Commons Briefing Paper – 'The Motor Industry: Statistics and Policy':
http://researchbriefings.files.parliament.uk/documents/SN00611/SN00611.pdf

House of Commons Business, Energy and Industrial Strategy Committee – Brexit and the Implications for UK Business automotive inquiry:
http://www.parliament.uk/business/committees/committees-a-z/commons-select/business-energy-industrial-strategy/inquiries/parliament-2017/inquiry1/

Lloyds Bank – 'Automotive Research Report 2017':
http://www.lloydsbankinggroup.com/globalassets/documents/media/press-releases/lloyds-bank/2017/170301-lloydsbank-automotivereport.pdf

PA Consulting Group:
http://www.paconsulting.com/

Society of Motor Manufacturers and Traders:
https://www.smmt.co.uk/industry-topics/brexit/

Society of Motor Manufacturers and Traders Motor Industry Facts 2017:
https://www.smmt.co.uk/wp-content/uploads/sites/2/SMMT-Motor-Industry-Facts-2017_2-online.pdf

For further information please contact:
Venson Automotive Solutions on 08444 99 1402,
email sales@venson.com or go to www.venson.com

@venson_Fleet

Venson Automotive Solutions Ltd
Venson House
1 A C Court
High Street
Thames Ditton
Surrey KT7 0SR
Tel: 08444 99 1402

www.venson.com

email: sales@venson.com

@venson_Fleet

Published January 2018