

The Impact of Brexit on German Businesses

Results of the IHK Business Survey
Going International 2018

Going
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2018



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DIHK's nationwide survey "Going International 2018" was created with support from 79 Chambers of Commerce and Industry (IHKs) in Germany. More than 2,100 German-based companies with foreign operations took part in the survey, which was conducted in February 2018. The results of this special analysis of Brexit are based on responses from around 900 companies with significant business contacts in the UK, representing 43 percent of total responses.

Form of business activities in the United Kingdom (share of companies)

Exports of goods and services to the United Kingdom	91%
Imports of goods and services from the United Kingdom	26%
Office/place of business in the United Kingdom	25%
We employ British nationals	19%

Trade volume between Germany and the United Kingdom (UK) amounted to EUR 121.5 billion in 2017. About 750,000 jobs in Germany depend in trade with the UK. To date, German companies have investments in the UK with a value of over EUR 140 billion, and maintain about 2,500 places of business in the UK with nearly 400,000 employees. There are 1,400 British companies in Germany, with about 240,000 employees.

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Key Results:

1. The upcoming Brexit is already a burden for companies

- German companies with business in the UK expect business to deteriorate once again in 2018.
- German trade with the United Kingdom is already decreasing significantly.
- One in every 12 companies is currently planning to shift its UK investments to other markets.

2. An unclear Brexit and a disorganized transition are creating uncertainty

- The details of the impact is still unclear for many companies since negotiations have failed to make substantial progress.
- Additional cost burdens from customs and taxes should be prevented if possible.
- Rapid clarification of the future relationship between the EU and the UK is indispensable. A possible transitional phase through the end of 2020 must also be clearly and transparently defined.

3. The benefits of a single internal market should be protected

- Free movement of goods within the internal market is the top priority for companies.
- Investments leaving the UK will go primarily to Germany and other EU countries.
- The internal market of the EU-27 should be further strengthened.

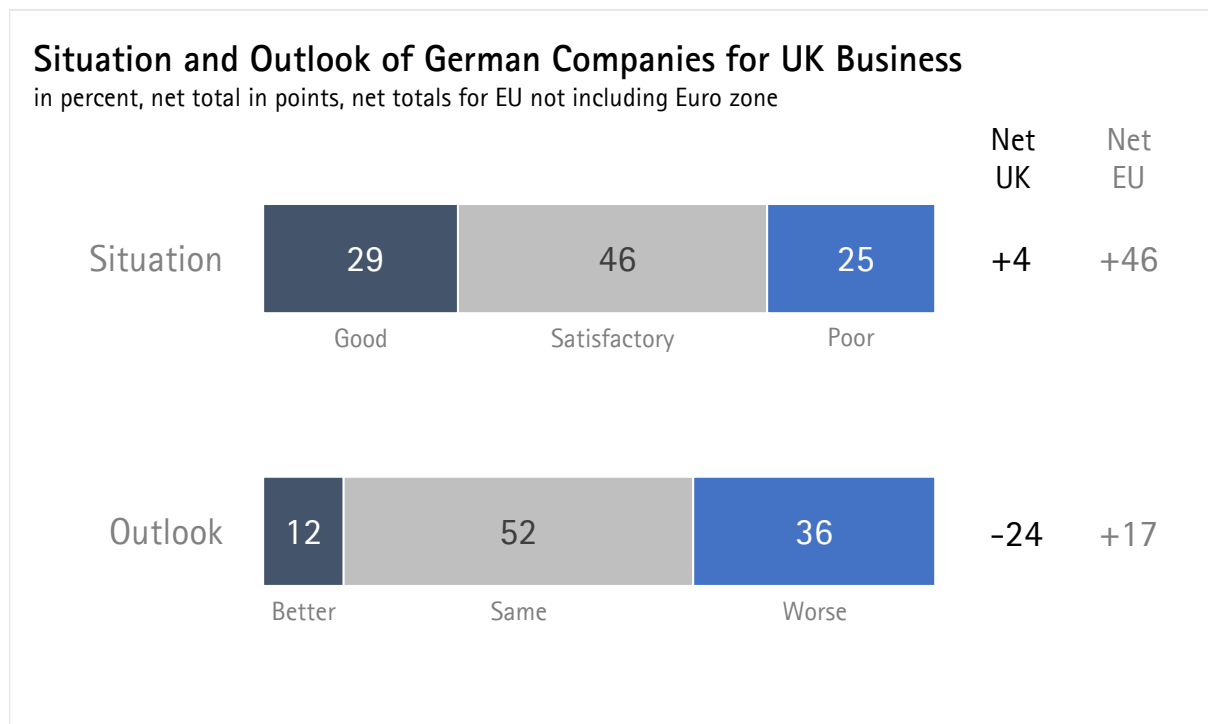
Company Assessments

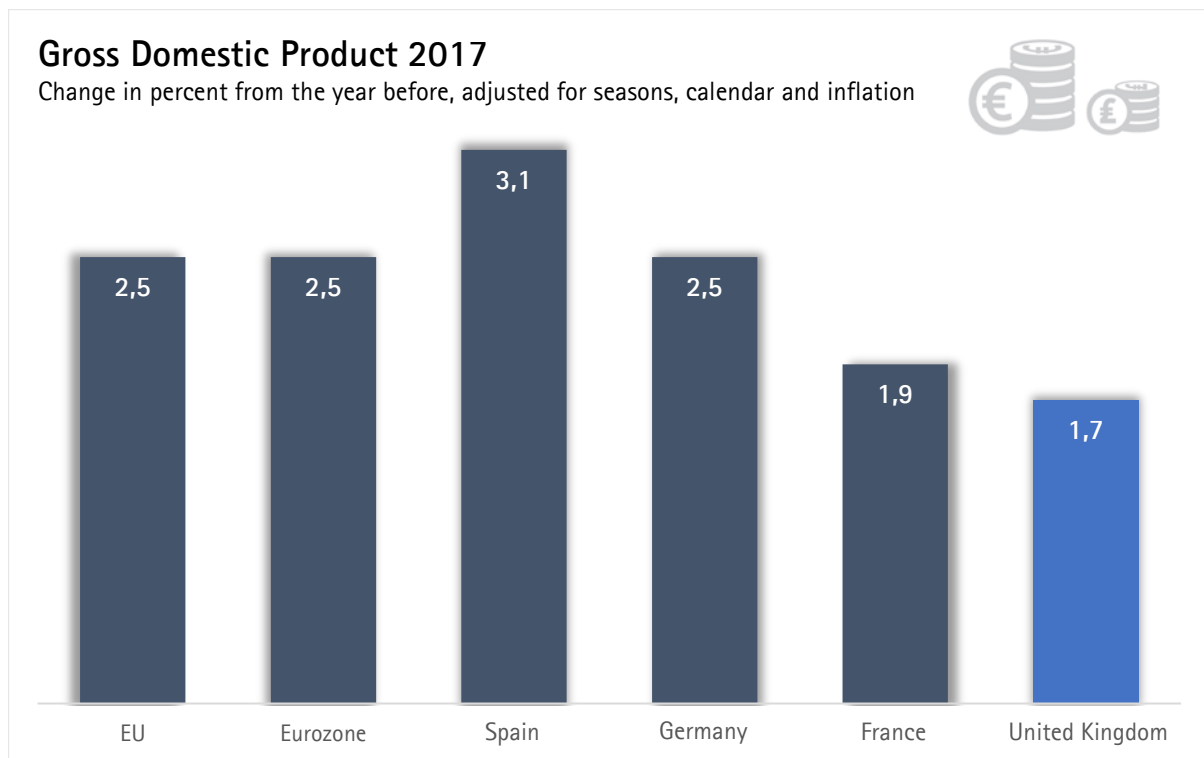
The impact on German companies of the departure of the United Kingdom (UK) from the European Union (EU) will be overwhelmingly negative in terms of business, investments and trade. The first signs of this impact are already noticeable: since the Brexit decision, trade with the UK has grown at a much less dynamic pace than it would be expected given the economic context. The specific ways in which conditions for business with the UK will change are still entirely unclear for companies. Almost two years after the referendum and one year after the British government gave notification of its withdrawal, the details are still unclear. A possible transitional phase could mitigate the negative consequences, but at the same time threatens to prolong the uncertainty. But some companies are already planning to shift their investments, primarily to other EU countries.

Companies expect business to deteriorate significantly in 2018

German companies with trade or investments in the UK assess the current state of their business to be somewhat satisfactory: 29 percent rate their UK business as good, but one in every four companies calls the situation poor. The net positive total has increased minimally from the last survey, from three to four points.

By comparison, German companies assess the current business situation with other EU countries with a net positive of 46 points, and the net positive for Euro zone countries is 65 points.





Companies expect their UK business to deteriorate significantly in the next twelve months, with pessimists (36 percent) much more numerous than optimists (twelve percent). This represents a net value of minus 24 points. Companies with imports from the United Kingdom are especially pessimistic (net total of minus 32). Viewed by sector, the metal industry, the automotive industry and suppliers and wholesalers are most pessimistic about their business outlook.

But companies are already feeling the impact of the upcoming Brexit. Since the referendum, the British Pound has fallen against the Euro, resulting in a loss of purchasing power in the UK and ultimately worsening the sales outlook for German manufacturers. German exports to the United Kingdom decreased by about two percent in the past year. Before the Brexit vote, the UK was Germany's third-largest sales market. In 2017, it was fifth.

British GDP growth is also not as strong as it was before the referendum, and is hardly keeping pace with growth in other EU countries. Based on the current company survey, DIHK expects

GDP growth of 1.5 percent in 2018, well below the EU average of 2.1 percent.

The consequences of Brexit are still unclear for many companies

Companies are trying to prepare themselves: about one year before the UK's official withdrawal from the EU, 79 percent of German companies, even those without direct trade relations with the UK, have already considered the potential impact on their business. Even without a direct supply relationship with British companies or investments in the United Kingdom, companies may be affected by Brexit indirectly via supplier structures, primary products or customer relationships.

For example, a manufacturing company currently purchases components exclusively from suppliers in Germany and France and may not consider itself to be affected by Brexit. However, if the components manufactured by one of these suppliers uses British primary materials, the affected component and possibly, by extension, the

The Brexit process

The guidelines for negotiations concerning the framework of future relations between the EU and the UK are to be adopted at the EU Summit on 22 and 23 March 2018. By the end of October 2018 at the latest, the Brexit negotiators will draft a proposal concerning the withdrawal agreement and detailed rules for the "transitional phase," which is expected to last through the end of 2020. This draft is to be presented to the European Parliament and to the British House of Commons for approval and is then to be ratified by the EU Council. The United Kingdom will withdraw from the European Union on 30 March 2019. Negotiation of an agreement concerning future relations in the period after the transitional phase is expected to take a few more years. As things currently stand, a free trade agreement between the EU and the UK is the most likely model for future relations.

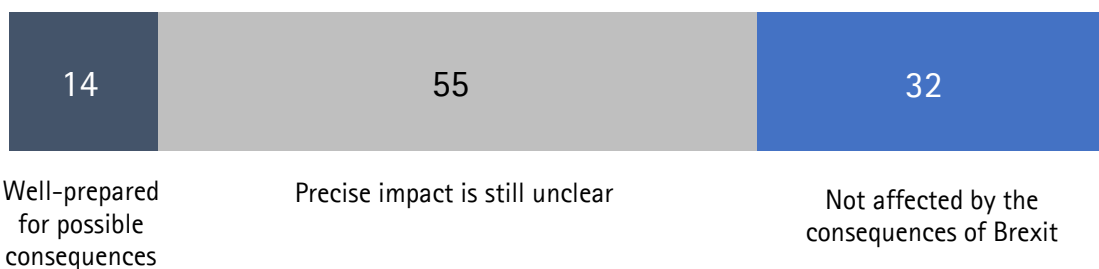


final product as well, may no longer be able to claim referential EU origin after Brexit and would therefore be unable to benefit, e.g. from the EU's trade agreements with Canada or South Africa.

percent have yet to analyze the potential impact on their business of the UK's withdrawal from the EU.

21 percent of German companies with foreign activities have not checked yet whether they will be affected by Brexit. Of companies which have direct and significant business with the UK, 15

Responses from companies which have considered the impact of Brexit on their business in percent



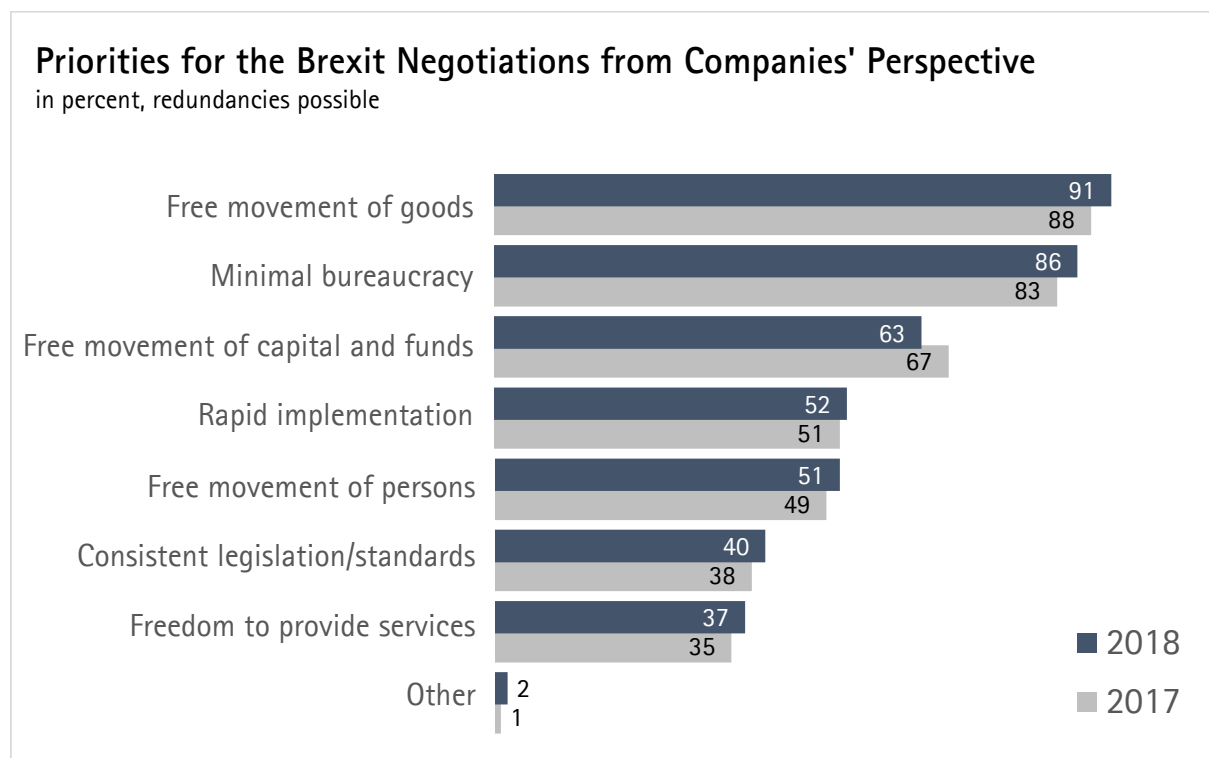
But of the companies which have been closely engaged with the impact of Brexit, only about one in every seven companies considers itself well-prepared for the possible consequences of Brexit. One third will not be affected by the consequences. However, more than one half of companies are still unable to assess the consequences for them even after in-depth consideration of the issue. The precise impact of Brexit simply remains unclear.

Breaking down the companies by size, small companies are most likely to say that they will not be affected by Brexit. Larger companies will be affected to a greater degree and are more likely to state that the precise impact is still unclear. Many details in connection with supply chains are extremely complex and particularly issues like customs procedures and technical approvals may play a decisive role in successful trade. If conditions are unclear, companies will be unable to operate with certainty and may even refrain from engaging in business because of the doubts. It is necessary to clarify relations

and conditions between the United Kingdom and the EU as quickly and completely as possible.

Priorities for companies in the Brexit negotiations

Companies' priorities for the Brexit negotiations have hardly changed since the last survey. The most important issue continued to be the free movement of goods: 91 percent of companies fear restrictions or higher costs for the delivery of goods. This is also associated with concerns about more bureaucratic requirements, such as customs declarations and approval procedures. 86 percent of companies view this as an important issue in the negotiations. A little more than half of companies doing business in the UK see rapid implementation as a priority for the negotiations, with the associated hope of having clarity about how Brexit will impact their business as soon as possible so that they can prepare for the consequences. In addition, one half of companies cite free movement of persons as an



important factor and at least one third of companies mention consistent laws and standards and the freedom to provide services.

The list of priorities makes clear that the EU's achievements, such as the free movement of goods, are extremely important to companies. Individual companies also point out that Brexit must not jeopardize the stability of the internal market in the remaining 27 EU countries. They warn against affording the UK too many privileges in the course of the negotiations. A few companies also have concerns about the future of the British Pound.

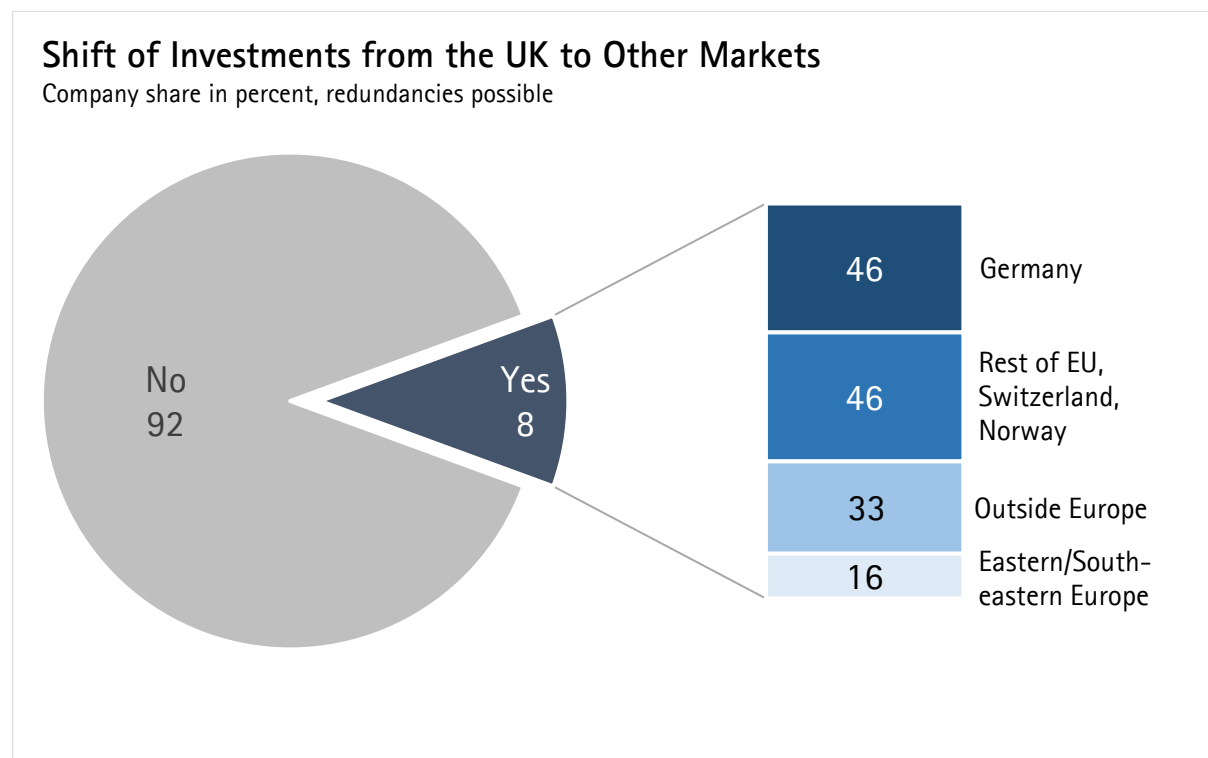
Shifting of investments

About eight percent of companies with investments in the United Kingdom are already planning to shift investments to other markets due to

the UK's upcoming withdrawal from the EU, despite the fact that the precise conditions of the withdrawal are not yet evident.

By shifting their investments, companies hope to mitigate the negative impact from loss of membership in the internal market. While shifting production will involve costs in the short term, withdrawing from the United Kingdom creates added certainty in a long-term perspective. It remains unclear which incentives the British government will adopt to attract investments after Brexit.

Since the benefits of the internal market will likely no longer be available after Brexit, German companies are planning to shift investments primarily to the internal market of the remaining 27 EU countries. About one half of companies are considering shifting investments to Germany, another EU country, Switzerland or Norway, while one third are considering a future target region outside of Europe.



Possible effects of Brexit on German–British trade: a customs related perspective

If the United Kingdom (UK) is no longer a member of the EU Single Market, all companies trading with UK must declare their goods to customs. DIHK estimates that at least 30.000 German companies that export to UK would be affected by this. Furthermore, around 40.000 companies will have to deal with custom declarations because they import from UK.

- Estimated number of additional customs declarations: ca. 14.6 Mio p.a.
- Estimated cost for total number of customs declarations: ca. 200 Mio. Euro p.a.
- Estimated cost for total number of preferential proofs of origin: ca. 300 Mio. Euro p.a.

These figures reflect a conservative estimation as they are based on surveys that asked companies which are rather familiar with filing customs declarations and making out preferential proofs of origin.

In this view Brexit will be especially harmful for two groups of companies:

- Companies that up till now only trade within the Single Market and therefore are not familiar with custom procedures. Often these are small or medium sized companies (SMEs).
- Companies with internationalized and complex production chains, which export and import numerous times for processing purposes before their product is completed. This requires a customs declaration each time.

Red tape and costs for filing customs declarations and making out preferential proofs of origin for German businesses in case (estimation by DIHK)

	Number of declarants* (economic operators)	Number of declarations p.a.* (customs declarations)	Costs for total number of customs declarations p.a. in Euro (assuming 40 Euro/h as wage = 14 Euro per declaration)**	Costs for total number of preferential proofs of origin p.a. in Euro (assuming 40 Euro/h as wage = 27 Euro per proof of origin)***
Import	39.489	4.609.313	64.530.382	93.338.588
Export	31.420	9.990.408	139.865.708	202.305.756
Total		14.599.721	204.396.090	295.644.344

* Estimation: Derived from data by Federal Statistical Office of Germany for United States for 2016; Correlation of goods portfolios between US and UK: Import 85 %; Export 95 %.

** Based on surveys by Chambers of Commerce and Industry (CCI) Rhineland-Palatinate, CCI Bavaria, own calculation by Association of German CCIs (DIHK)

*** Assumptions: Proof of origin via formal preferential Certificate of Origin. Utility rate of customs preferences under possible EU-UK Free Trade Agreement of 75 %. This means for 75 % of all shipments economic operators will declare preferential origin in order to benefit from e.g. 0 % customs duty on import / export. Costs for preferential proof of origin on import will be covered by British companies, but are likely to be forwarded on to German importers.

Source: Federal Statistical Office of Germany, CCI Koblenz, CCI Munich, DIHK