Brammer Buck & Hickman

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White Paper

Brexit:
The Seven Major Risks To The Continuity Of Your Production Line That You Haven't Considered

And How To Deal With Them

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Executive summary

The United Kingdom is set to leave the European Union on 29 March 2019.[1] As a UK-based manufacturing business, this will undoubtedly threaten your production line and access to stock and industrial supplies, especially with a 'Hard Brexit' looking increasingly likely.

Nearly two-thirds of UK companies have still not carried out a risk assessment on the impact of a 'No Deal Brexit'.

So much about Brexit is uncertain, yet despite this, nearly two-thirds of UK companies have still not carried out a risk assessment on its impact.[2]

Consequently, large parts of the British economy are not ready for such an outcome.[3] Many manufacturing organisations are struggling to create a clear plan of what they need to do to minimise the impact of Brexit and maintain production output levels to satisfy customer demands.

The seven biggest risks of Brexit

- Economic and financial risk
- Supply chain
- Customs compliance
- New routes to market
- Tariffs
- Services not covered
- Continuity of production

[1] 'Leaving the European Union', *Parliament UK*
[2] 'Most U.K. Businesses Aren't Preparing For Brexit Yet, BBC Says', *Bloomberg*
[3] 'Brexit: UK Economy Not Ready For No Deal, Mark Carney Says', *BBC News*

The potential threats to production line continuity you need to consider

With the Prime Minister's proposed deal having been voted down by Parliament, a 'No Deal' (or 'Hard') Brexit is quickly becoming one of the most probable outcomes. This will likely see the UK exiting the EU with no agreement on our future trading relationship, forcing the UK to revert to World Trade Organisation (WTO) rules.[4]

Should this occur, the risks to the continuity of your production line would be huge, with all temporary customs agreements existing between the UK and the EU no longer valid. Instead, the UK would be forced to follow the same customs checks and tariffs as other WTO countries such as Australia and Argentina, with grave uncertainty on how both exports and imports into the UK would be processed. The UK would need to establish its own global trade agreements, as all existing agreements would immediately be invalid. With these deals taking years to establish, this would mean more rigorous border checks on all imports for an extensive period of time whilst deals are negotiated.

As a result of this scenario, we will see a backlog of late deliveries, preventing your production line from running efficiently. Inefficiency means an increase in downtime, costs and customer complaints, which in turn could lose you future orders - especially if a competitor is able to fulfil an order when you can't.

> *Hard borders will see a backlog of late goods required to maintain your production line and customer commitments*

Economically, the British pound may become a risk currency for a period of time, causing it to fluctuate in value amidst the uncertainty. Investment from outside the UK will decrease alongside the risk of depletion in investors' assets.

Transactions involving the British pound will see an increase in the cost of raw materials and industrial supplies to compensate for this depreciation. Detrimental impacts on the economy and trade are expected, with additional customs checks and border controls bringing disruption to major manufacturers.

In contrast, a 'Soft Brexit' would enable close ties to be maintained, post-Brexit, between the UK and the EU, with mutual agreements in place on key areas such as trade, skilled labour migration, tariffs and trade restrictions.

[4] 'What If There's No Brexit Deal?', *Parliament UK*

Whilst the impact of a 'Hard Brexit' would be more severe, these 'mutual agreements' for a softer Brexit would still differ to current trading rules and regulations. As such, manufacturers will need to endure changes to their production line processes no matter what the outcome of Brexit – especially those manufacturers reliant on imports from the EU.

There are five scenarios that could form part of the outcome of the current political turmoil. They are:

1. The 'No Deal' scenario highlighted above
2. A free trade agreement
3. Customs union
4. Single market, or
5. The possibility that Brexit is stopped altogether

With such high levels of uncertainty surrounding the outcome, and with so much riding on the decision, UK businesses are strongly urged to prepare for the worst-case scenario: a 'No Deal Brexit'.

The seven key risks you need to prepare for

There are seven key risks to manufacturers that Brammer Buck & Hickman has identified and is mitigating for a large number of UK businesses already.

1. Economic and financial risk

With Brexit negotiations making the British pound a source of speculation on an international scale, any currency fluctuations will impact the price of all imports quite dramatically.

Forecasts for the impact of a 'No Deal Brexit' suggest that the pound will fall, with Credit Suisse going so far as to suggest that the UK could experience a "short-term recession", with a GDP contraction of between 1 and 2 percentage points. Capital Economics further forecast that GDP growth would fall to -0.2 percent in the case of a disorderly 'No Deal Brexit'.[5] Currency cost will, in turn, not only impact raw material costs for manufacturers, but also maintenance spares to keep their production lines running. A fall in GDP will ultimately impact order books.

[5] 'How No Deal Brexit Would Hit UK Economy', *Politico*

2. Supply chain

Increased complexity and cross-border duties and regulations will in turn lead to increased costs and inventory management challenges for UK businesses. The amount of work required to manage this is likely to increase significantly due to the additional paperwork required for every customs entry, impacting the supply chain costs (MSS reporting and deferment account management), as well as the time taken to pass between borders.

Companies and customs officials will not only have to deal with a vast scale of change, but also an exponential increase in expected error rates and fines. As these unfamiliar processes are dealt with, increases in delays and errors at customs will in turn see an increase in delays and costs to your production line. This will affect your ability to meet your customer demand, with more of your resources required to deal with complaints, in addition to the maintenance of your stock and production line.

Recently, the UK Department for Transport conducted tests over a 20-mile route leading up to the Port of Dover in the case of a 'No Deal Brexit', which would see the likelihood of mass queues on both sides of the border. This test-run involved a convoy of fewer than 100 lorries, which, when considering that over 10,000 lorries pass through the UK Channel ports every day, has led many to query its reliability.[6]

Customs delays of just 30 minutes could bankrupt one in ten firms, with impacts to firms, large and small.

3. Customs compliance

Under WTO rules, the UK will not have a frictionless border with the EU; exporters would have to prove they meet all of the EU's product standards and regulations. As a result, customs compliance may lead to inflated costs, delays to border crossings and an increased head count for customs paperwork. All of which will have a dramatic impact on the time taken to fulfil orders. Slower delivery also means more time between your manufacturing and delivery, ultimately delaying invoicing and payment. This will have a considerable impact on working capital.

Just last month, a Chartered Institute of Procurement and Supply (CIPS) survey found that almost a quarter of 1,300 surveyed firms are stockpiling goods for fear of border delays and shortages.[7] The survey went even further, stating that customs delays of just 30 minutes would bankrupt one in ten firms, regardless of firm size.

> *Only recently, car maker Honda went on record to state that a 'No Deal Brexit' could add 60,000 extra pieces of paperwork for imports and exports, costing millions of pounds.[8] In preparation, Honda has planned a six-day shutdown of its Swindon factory in order to ready itself for the disruption caused by Brexit.*

[6] 'Brexit: Operation Brock lorry park A256 trial 'too little too late'', *BBC News*
[7] 'Customs delays of 30 minutes will bankrupt one in 10 firms, say bosses', *The Guardian*
[8] 'Honda: No-deal Brexit 'would cost tens of millions', *BBC News*

4. New routes to market

In order to reduce the impact of some of these threats, the avoidance of logistical 'pinch points' may require sourcing from alternative producers, thereby affecting the brand offering.

5. Tariffs

As a result of Brexit – which will affect the whole of Europe, not just the UK – the cost of raw materials is likely to increase, which will in turn lead to price increases for UK manufacturers. This will inevitably see price increases for products and services whether for UK-based customers or exported back to the EU. In the event of a 'No Deal Brexit' and a fall back onto the UK's membership with the WTO, the UK would be subject to potentially higher trade tariffs.

Every WTO member has a list of tariffs and quotas (limits on the number of goods) that they apply to other countries, otherwise known as their WTO schedules. While in some sectors this is relatively low, in other sectors such as automotive, for example, it is adversely high, being taxed at as much as 10% for every time raw materials cross the UK to EU border. Even more disconcertingly, the food and beverages industry could see custom duties as high as 35%.[9]

WTO tariffs can range from 1%, to as high as 35%.

6. Services not covered

WTO rules barely cover trade within the service industries, which means that for those services not covered, there is even more uncertainty. For example, trading on only WTO terms would mean there would be no deal on air transport. In order to have access to the EU single aviation market, airline companies are required to have their headquarters and majority shareholdings in the EU, resulting in the potential for airlines to have to relocate.[10] Airbus, for example, have expressed concern over non-tariff barriers, which could result in additional customs procedures and bureaucracy, complicating supply chain processes and increasing costs.[11]

7. Continuity of production

In addition to all of these points – and perhaps also as a result of them – there is a real threat to continuity of production. Your ability to maintain the integrity of your production line and your commitments to your customers is directly impacted by your access to industrial parts. If you can't get those parts as and when you need them, your business will simply grind to a halt.

A Brexit scenario that imposes any type of additional tariff and customs barrier means that you may not have enough maintenance stock to actually cope. With an estimated 53% of all UK imports in 2017 coming from the EU, stock maintenance following Brexit will become critical in planning for likely stock and parts shortages.[12]

[9] 'World Tariff Profiles 2017', *World Trade Organisation*
[10] 'No deal? Seven reasons why a WTO-only Brexit would be bad for Britain', *The Conversation*
[11] 'Airbus outlines Brexit risks to UK facilities', *Flight Global*
[12] 'Statistics on UK-EU trade', *Parliament UK*

Five Brexit Scenarios To Consider

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1. No Deal

The UK would default to operating under World Trade Organisation (WTO) rules.

Increased border control

Increased admin for the movement of products, goods and services between the UK and EU will see increases in costs, time, and ultimately affect continuity of production.

Tariffs

WTO tariffs depend on the product or service, varying from 2.6% for non-agricultural goods to 35% for food products, impacting both imports and exports.

Customs compliance

The WTO and EU have varied product and food safety standards, adding extra steps to current processes to accomodate these differences.

Services not covered

The WTO rules focus on the movement of goods and have limited, or no, legislation for other services e.g. banking and aviation.

Enforcement of WTO rules

Just as the EU doesn't abide by all WTO rulings within the EU, the EU can pick and choose what it allows the UK to sell in the EU, with disputes often difficult to settle.

Trade deals

Concerns with the WTO has led to countries, such as China and the US, to set-up their own trade deals. The UK would need to broker their own deals, which would take time to put in place.

Other Brexit scenarios:

2. Free Trade Agreement

- Zero duty applied on products that meet qualifying criteria with all others subject to 3rd country duty rates.
- Real life examples: Canada, Mexico.

3. Customs Union

- Customs Union with the EU, but not in the Single Market.
- Real life example: Turkey.

4. Single Market

- In the Single Market but not in the European Economic Area.
- Includes the free movement of goods, services, capital and people.
- Real life example: Norway.

5. Brexit Stopped

- UK continues to operate in the EU as per current terms & operating environment.

Risk assessment & mitigation

If you are to mitigate the risk to your continuity of production, you need to be aware of the impact Brexit could have on your manufacturing line no matter what the outcome, so that you can prepare for those risks by implementing robust tailor-made solutions.

By way of example: recently, we worked with a UK customer, helping them to understand the potential impact of Brexit to their business. From their risk assessment they were shocked to find that over 60% of their industrial supplies are currently sourced from the EU. This means that spare part availability will be reduced, they will not have adequate industrial supplies to cover their needs, and they will experience more stock-outs. Stock-outs, in turn, mean disrupted manufacturing lines, lower productivity and higher costs.

They concluded that if they don't act, they will see an increase in downtime and, as a consequence, incur additional costs of up to £2m next year. This is before they have even considered overtime costs, recruitment cost for temporary labour, penalties for late deliveries or, in the worst case, lost customers.

It is clear that in this example, as well as in many other cases that we have worked on, the key to mitigating these risks as best as possible is all in the planning. Proper planning provides you with the confidence that, regardless of the outcome of the ongoing Brexit issues, your business is prepared, and you do not have to worry about the availability of industrial supplies to maintain production and fulfil your customer obligations.

Brexit and your production line - the Brammer Buck & Hickman solution

We are working with our customers to mitigate these risks and provide bespoke solutions in order to deal with any procurement issues, concerns and challenges in relation to maintaining the integrity of their product lines. We can do this because:

- Of our extensive understanding of the industrial supplies supply chain
- We are part of the Rubix Group network, who have businesses across the UK and the EU
- Of our stock-holding expertise

In October 2018, we carried out a detailed Brexit-Readiness survey of our suppliers. In each case the survey clarified:

- Country of origin
- Country of shipment to the UK
- HS codes for the product (The Harmonized Item Description and Coding System)
- Delivery route to the UK
- Inventory risk mitigation

The resulting dataset allows us to make recommendations and plan for the various logistical impacts a 'No Deal Brexit' will bring, together with alternative supply chain options.

We are ready for Brexit, and we want you to be ready too.

Our knowledge and experience means we are equipped to help you immediately, not only as a single source supplier of industrial supplies, but also with a common-sense approach to your own Brexit preparations. Our supply chain expertise will help you identify key risks related to your industrial supplies availability, make recommendations based on your industry sector and build a robust stock-holding solution to suit your specific needs, whilst minimising your initial outlay.

> *In one instance we have already analysed their industrial parts data and made recommendations to increase their stock levels to support an additional three months' worth of production capability.*

We are working with a number of large businesses and supporting their Brexit risk assessments. In one instance we have already analysed their supplier data and made recommendations to increase their stock levels to support an additional three months' worth of production capability.

In addition, we are also able to draw upon the significant stock-holdings of the wider Rubix Group businesses to offer alternative product ranges sourced from outside the EU, giving our customers appropriate alternatives and as much peace of mind as possible.

Taking action

We have developed a diagnostic tool to highlight how ready you are for Brexit.

To run the diagnostic tool, simply click on the link below, or alternatively speak with us directly by calling your local branch to discuss the next steps in protecting your business, your production commitments, your customers and ultimately, your bottom line.

Your Brexit Risk Assessment Starts Here

www.bit.ly/BBH-Brexit-Diagnostic

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