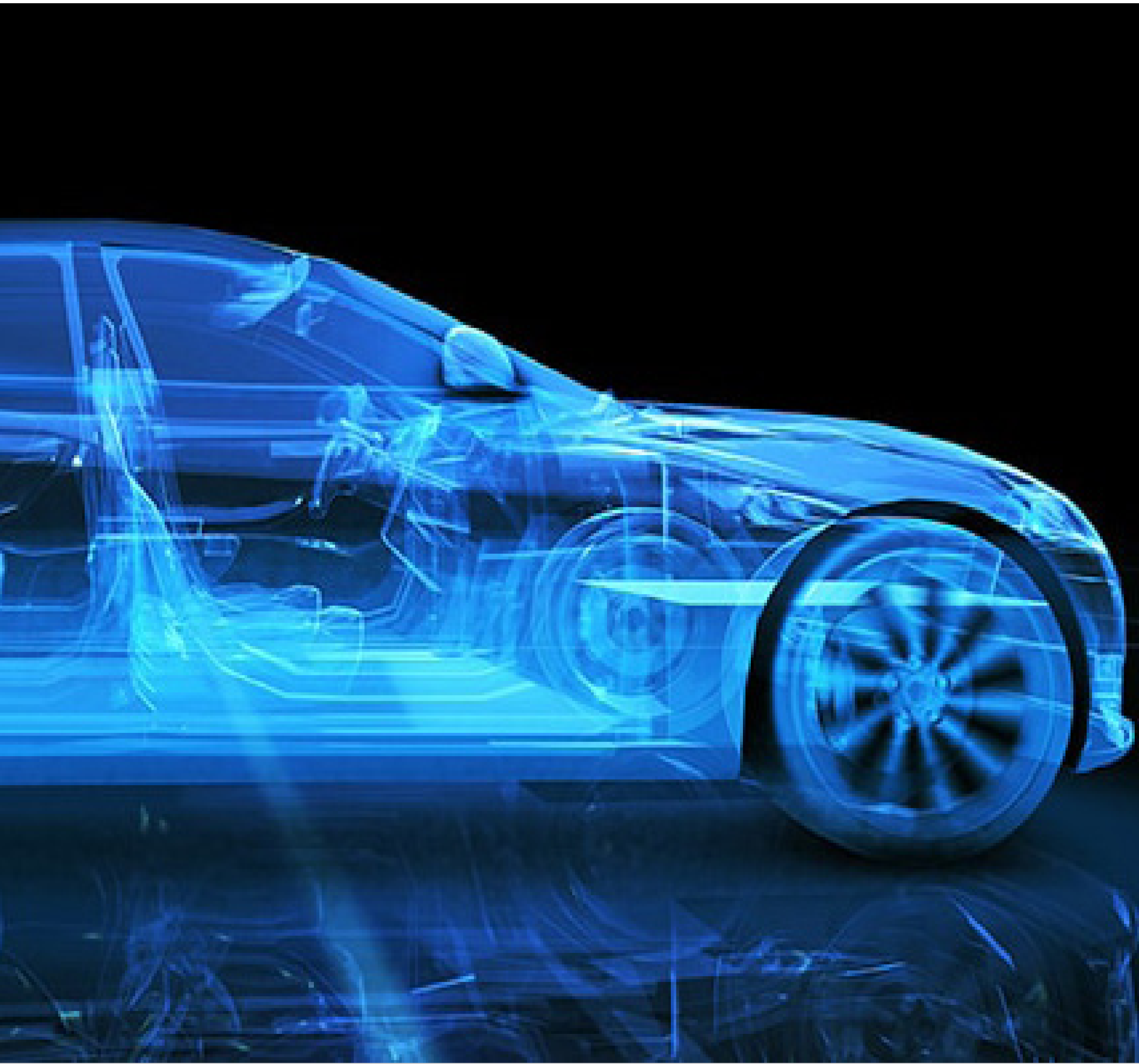
US-China Trade War and Impacts on the European Auto Industry



In 2018, the auto industry globally faced flat sales and now, on the first anniversary of America's trade war with China, it is nearly impossible for most global companies to be immune to the wrath of the U.S. Even with some organisations re-routing supply chains or expanding domestic manufacturing for local consumption where possible, the shockwaves are being felt by all.

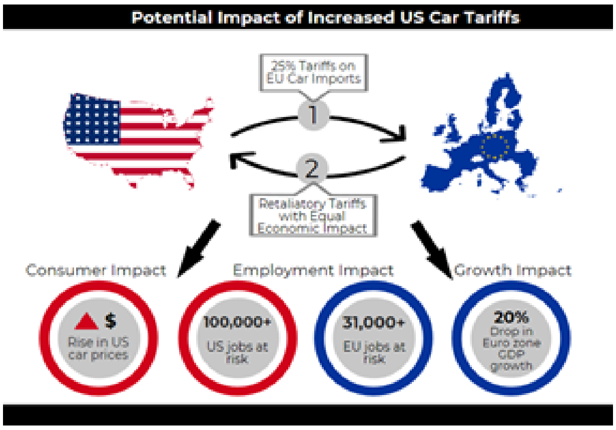
With the potential implementation of 25% tariffs for vehicles imported to the USA, European car manufacturers are caught in the crosshairs. This is in addition to the headwinds from the implementation of worldwide harmonised light vehicle test procedure (WLTP), evolution of driverless cars, increased investment requirements for R&D, the surge in ride hailing popularity and general shifts in consumer buying behaviour. The result is an unprecedented time of change for the auto industry – especially in Europe.

As the auto industry has the world's most complex and far reaching supply chain ecosystem, mitigating risk and pivoting production are herculean tasks. However, shifts must be implemented and imminently. The digitalisation of supply chains should be a key global CEO agenda.

Europe is home to 40%[1] of the world's leading auto manufacturers and in 2018, 22% of all cars sold in the United States were of European-owned origin[2]. Whilst Europe imposes a 25% tariff on imported American vehicles, the reciprocal tariff by the US would have a significantly different impact. The Munich-based Institute for Economic Research warned that German auto exports would fall as much as 50%[3] as a result of the introduction of US tariffs, and would decrease imports of vehicle parts into the EU. Adam Posen, President of the Peterson Institute for International Economics, estimated that tariffs would raise auto prices by 9% and would cut the global industry's output by 1.5%, costing 195,000 jobs[4]. The President of Germany's DIHK Chambers of Commerce estimates that US tariffs on imported cars would slash around €6 billion ($6.99 billion) off German economic output[5] alone. With Nissan announcing a 94.5% fall in net income for the first quarter of 2019[6], the net impact across Europe is less than promising.

Already faced with the impacts of the steel tariffs, China car consumption slowdown and the US/China trade war, one leading Tier 1 global automotive supplier headquartered in Asia is rapidly developing its digital supply chain capabilities. By creating a hub of cross-functional experts from supply chain, I.T, trade and compliance and manufacturing, they will execute the complexities of optimising the conversion of cash and claw back critical net margin. Cassandra Lee, Partner in the H.I. Executive Consulting Hong Kong office shares that this is a recurring theme not only amongst the Tier 1 parts suppliers, but all facets of the supporting sector. "The challenge most are facing is identifying exactly how to digitalise their supply chains which have a combination of legacy MRP, ERP, PLM, WMS, TMS systems and hybrids. They have dynamic tariff rates, long lead times, high value inventory and manufacturing and distribution in 20+ countries and the need for real time accuracy. It's not a unique situation as some industries and complex global organisations had travelled this path and long before the term 'digital supply chain' – yet it is critical to know who has evidence of delivering this transformation and what success looks like. In fact, most organisations struggle to identify what a 'digital supply chain' is, let alone know how to implement it. High yield talent in this space is in high demand and compounded in Asia by factors including Dyson's headquarter move to Asia and development of their electric vehicles business unit."

The WTO reports that the US-China Trade war is directly impacting 3% of global trade , with the global auto industry accounting for 8%. Goldman Sachs recently reported, “The GDP impact of the tariffs implemented to date remains small at about 0.1 percent for the Euro area. But we estimate that the cost would rise to 0.3 percent of the Euro area GDP, if the trade war were to escalate to include auto tariffs”. Further, spill overs from the auto industry into other segments could amplify the losses to production. “Hence, the indirect effects on other sectors nearly double the effects in Europe” adds Goldman Sachs.



Source: US-EU Auto Tariffs: What's at Stake? Atlantic Council, 14 June 2019

An Austrian-based industry leader shared, “If the supplier industry has 10-20 customers in different regions, the risk of being dependent on one customer is largely minimized. Therefore, one could expect only a maximum economic loss of 10-15% during such a crisis, this assumes that not only the customer structure is balanced but also the revenues per customer hold. Even if US power politics continue the US will not be able to hold China back as a rising economic power.”

With only four months remaining until the fate of the EU targeted tariffs is decided, a leading European global supplier shared with Theda Von Sperber from the HIEC Munich office, “There is a fear of executing further investments by the automotive industry. This restraint has a meaningful impact for medium-sized automotive suppliers and led to a 15% drop in sales. Chinese investors are a positive addition to the industry, although they are not currently investing in Europe's auto industry.” Additionally, the sentiment of local manufacturing for local consumption is echoed across Europe with a strong rise in demand for global digital supply chain talent to create and implement this strategy to claw back whatever margins possible.

The World Trade Organisation’s chief economist, Robert Koopman shared that “US tariffs on the car industry would have a much bigger effect on the global economy than the trade war between the US and China”. In 2017 total global trade was worth US$22 trillion, with direct trade between the US and China accounting for just 3%, compared to 8% for the car sector including parts. Koopman reiterated the investment fears, warning “The big danger of these kinds of tariffs is that they cause investors and consumers to hold off on spending, and you get a bigger macroeconomic negative effect.” The US-based Centre for Automotive Research states that its worst-case prediction showed such a tariff would lead to nearly 370,000 job losses in the car industry and 1.3 million fewer car sales a year.

Whilst Vietnam and other South East Asian countries are seeing gains from the ongoing US-China trade war in other sectors, there may be no winners when it comes to the Automotive industry being caught in the crossfire.

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> – Robert Koopman, WTO”

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