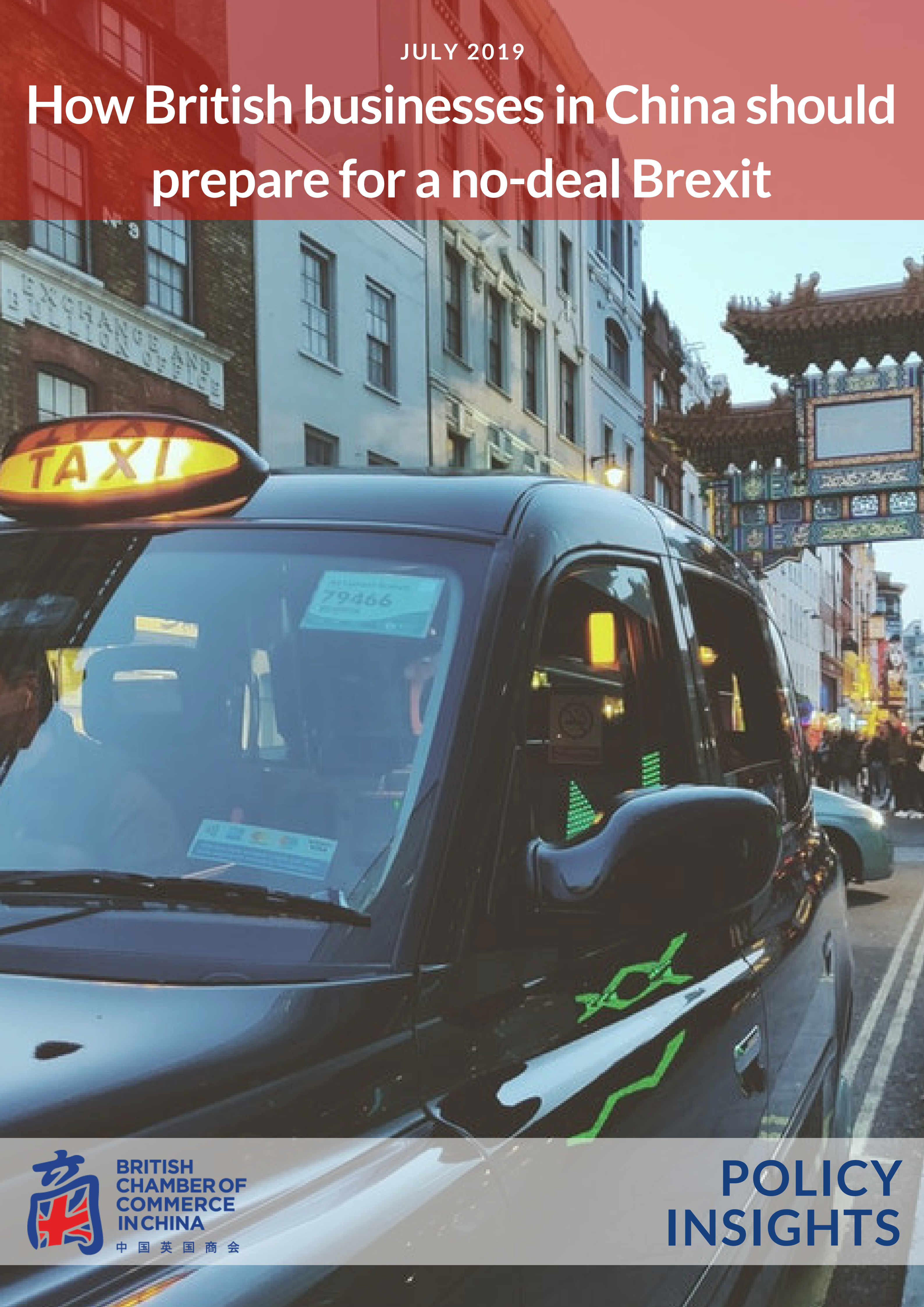
JULY 2019

How British businesses in China should prepare for a no-deal Brexit



BRITISH CHAMBER OF COMMERCE IN CHINA
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POLICY INSIGHTS

HOW BRITISH BUSINESSES IN CHINA SHOULD PREPARE FOR A NO-DEAL BREXIT

The UK is scheduled to exit the European Union on the 31st October 2019. With the final two Conservative Party leadership candidates, Boris Johnson and Jeremy Hunt, refusing to rule out the possibility of a no-deal Brexit, British businesses must now prepare for the potential subsequent fallout.
A no-deal Brexit would mean the end of the UK's access to the European Single Market and Customs Union, replaced by alignment with World Trade Organisation rules on cross-border trade.

Continued uncertainty over a future Brexit deal has shaken business confidence in the UK, with 22% of firms reporting plans to reduce investment in the UK and 20% planning to move capacity to mainland Europe.[1] However, British businesses largely believe that their China operations are insulated from the potential effects of a no-deal Brexit, with 56% of members reporting that they expected there to be no impact from a no-deal Brexit on their China revenues and only 24% expecting their business to be negatively affected, according to the Member Sentiment Survey[2] produced by the British chambers of commerce in China.

Are businesses right to feel removed from the ripple effects of a no-deal Brexit scenario? We consulted with several client services firms with expert knowledge on the subject, who gave the following advice for businesses to re-evaluate their assessment of insulation from Brexit.

1. Know your supply chains

The main disruption to businesses caused by a no-deal Brexit will be to their supply chains when sourcing products and components from the EU, especially when concerning perishable, defence-related, or other highly regulated goods. While many business leaders in China may believe that their supply chains will be unaffected or have been sufficiently adjusted, it's important to make sure that your suppliers aren't also expecting elevated costs in a no-deal Brexit scenario.

Supply chains are often more complex than managers initially realise, says Michael Moore, Senior Brexit Advisor at PwC, who advises companies to thoroughly map out every link in their supply chain to identify possible areas of exposure and make sure this is carefully communicated to offices in all locations. Potential risks might include delays at customs and double taxation on any goods first coming into the UK from Europe, which would impact businesses in China if their supply chains are implicated. Even if employees in China fully understand their sources, it is important to pass this knowledge back to the UK so that supply chains can be altered and business plans adjusted to absorb any external costs. Finally, whatever the eventual outcome, taking the time to reassess operations should be seen as an opportunity to re-strategise, restructure and streamline supply chains, both mitigating risk and optimising business performance, according to Tom Rathborn, Brexit specialist at Grant Thornton.

2. Keep on top of changing regulations

A no-deal Brexit also brings uncertainty to the type of legislation governing UK business operations after the exit. The sweeping shift in regulation that could immediately follow a no-deal Brexit would have a real impact on UK headquarters when making decisions about everything from tax assessments to data-sharing regulations in its China operations.

This is particularly critical for firms in import-export industries. Businesses should make sure they are informed about the new rules of origin for anything imported from the UK to China and have all the appropriate procedures and documentation in place, and that they review any new requirements established by new trade agreements negotiated by the government. In our consultations, one expert from a major international logistics firm recommended ensuring that businesses compile and maintain a master database to stay on top of the tariff codes assigned to their products or imported supplies, in order to facilitate reviewing increases or drops in tariff rates in the wake of trade agreements. Equally important is to stay abreast of developments on updates in standards to product labelling, packaging and so on.

3. Check your consumer markets

Upon leaving the European Union without a deal, British companies with a significant European consumer base will be immediately subject to the default tariffs the EU places on all external markets with which its members do not have Free Trade Agreements, lowering demand for British goods within the EU.

The knock-on effects on revenue for a business' UK headquarters could lead to them lowering their projected investment into China to guard against cashflow or revenue issues. Businesses operating in China should ensure therefore that they maintain close communication with their head office on future planning throughout the post-Brexit adjustment period. Even if British businesses in China are confident that they will not be heavily impacted by a no-deal Brexit, Duncan Levesley, of Grant Thornton’s China Britain Services Group, nevertheless advises them to clearly communicate with customers and staff about why they will not be affected, citing one firm that lost business because they failed to reassure a client that they would not be adversely affected post-Brexit. To gain an understanding of how a potential slump in GDP may play out, Mr Rathborn advises that organisations review the impact of the global financial crisis on their operations and establish if there are any lessons to be learned.

4. Watch the exchange rate

It remains unclear what form the UK's post-Brexit international trading relationships will take, presenting a key challenge for business. The lack of available information makes it difficult for firms to assess their future strategies, and misguided investment choices could have a serious impact on the success of overseas ventures. Market jitters in the wake of Brexit are likely to lead to a drop in the value of sterling, which reduces the purchasing power of companies in the UK. However, this should not directly affect operations in China and may also be an opportunity as it will reduce the price of UK exports. Duncan Levesley points out that cheaper assets can also make the UK a more attractive destination for foreign investment.

5. Don’t expect too much from an FTA

The prospect of the UK signing its own Free Trade Agreements with other major economies such as China is often considered an attractive proposition for business. However, Mr Levesley cautions that an FTA may not address many of the core issues British firms face in China. He reports that his clients’ key obstacles to business tend to be non-tariff barriers such as the complex legal and tax framework, competing and overlapping regulations, and IP concerns for example, which an FTA will not clearly resolve. Businesses should instead continue to advocate through their respective Chamber of Commerce on the pertinent issues that hinder their access to markets in China, and call for more practical support from government.

While the large majority of British businesses in China are unlikely to see drastic declines in performance after Brexit, it is nevertheless vital that companies check every aspect of their compliance policies and every link in their supply chains to safeguarded their business against a no-deal. Regardless of the probability of a no-deal Brexit, businesses should take every step to guard against any potential consequences. Those that do will be more ready to weather any volatility arising from a no-deal Brexit, and can capitalise on a potential opportunity to re-strategise and streamline their operations which will benefit their business, whatever the result.

[1] '6 MONTHS TO BREXIT: Investment and recruitment cut if ‘no deal'', The British Chambers of Commerce, September 2018. https://tinyurl.com/y6l66gzg

[2] 'British Business in China: Member Sentiment Survey', The British Chambers of Commerce in China, December 2018. https://www.britishchamber.cn/en/advocacy-en/

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