

The Impact of Brexit on German Businesses

Results of the IHK Business Survey
Going International 2017

2017



Impact of Brexit on German Companies

Summary

In the estimation of German companies, the withdrawal of the United Kingdom from the European Union will represent a significant drag on the trade of goods and services. The business outlook of companies which are engaged in trade with the United Kingdom is worsening significantly, as expected cost burdens due to taxes and tariffs and increasing bureaucratic hurdles at Europe's new borders will negatively affect business on both sides. The magnitude of this effect largely depends on negotiations between the United Kingdom and the EU. Regardless of the specific outcome of these negotiations, almost one in every ten companies is already planning to shift investments away from the UK because of Brexit and towards Germany or other countries within the EU internal market.

Uncertain times

The first effects of the Brexit vote are already being observed: German exports to the United Kingdom were down by a good 3.5 percent last year, particularly due to a slump in the second half of the year. Because of the negative impact on the economy, the British government is planning to conclude a free trade agreement with the EU which is intended to facilitate access to the internal market. Experience has shown that the negotiation of such agreements can take several years. As a result, companies in the UK, and in Germany and Europe as well, will lack certainty for a long time about the conditions under which they will be able to trade with and invest in the United Kingdom in the future.

Key trading partner

The United Kingdom is Germany's fifth-largest trading partner. Trade volume in 2016 amounted to 122 billion Euros. The UK is actually the third-largest market for German exports, with 86 billion Euros in exports in 2016. About 750,000 jobs in Germany depend on trade with the United Kingdom. To date, German companies have built production sites and businesses with a value of 121 billion Euros in the UK. German companies maintain about 2,500 branch offices in the UK, which employ nearly 400,000 workers. British companies have 1,200 branch offices in Germany, which employ about 220,000 workers.

DIHK's "Going International" survey

DIHK's nationwide survey, "Going International 2017," was conducted with the assistance of 79 chambers of commerce and industry. A total of 2,200 companies based in Germany with foreign operations took part in an online survey in February 2017. The results of this analysis of the impact of Brexit are based on about 1,300 responses from companies which do business in the United Kingdom. This represents 59 percent of the companies surveyed.

Companies' Assessments

Consequences of Brexit

The negotiations for the United Kingdom's withdrawal from the European Union will represent a major course change for German companies with international operations. Even shortly after the referendum, a clear sense of uncertainty was evident among companies.¹ The results of the DIHK survey, "Going International," show that this uncertainty has resulted in a significant worsening in the business outlook. Among companies which do business with the United Kingdom, 90 percent export goods and services to the island. About one third maintain establishments there in the form of production or distribution sites. 22 percent use the United Kingdom as a source of imports.

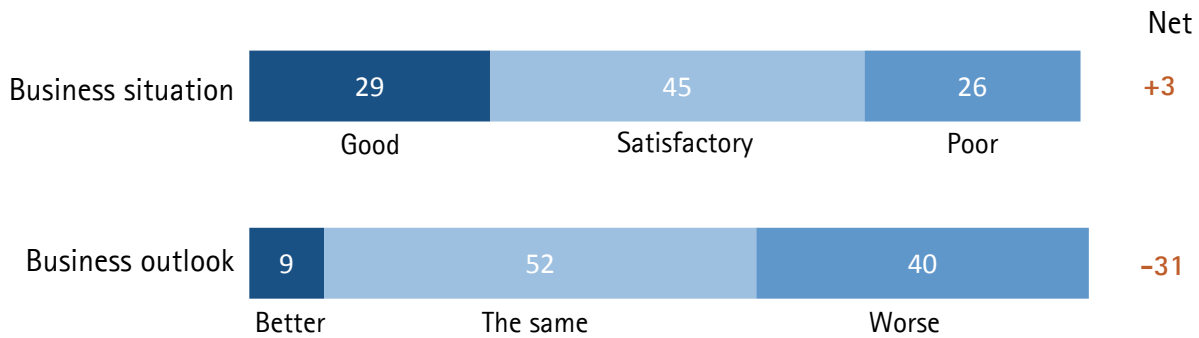
Form of business activities in the United Kingdom (percentage of companies)	
Exports of goods and services to the United Kingdom	90%
An office/branch office in the United Kingdom	26%
Imports of goods or services from the United Kingdom	22%

Pessimism reigns

Companies are very cautious in their assessment of the current economic situation. Companies rate the present business situation as somewhat solid, with a net positive value of three points, but expect business to get much worse in the coming months, with a net negative value of 31 points. This represents the worst value of all the regions examined in the Going International survey. Companies foresee major difficulties for the United Kingdom once it leaves the internal market and the most recent data pointed to flagging growth in the UK: 2016 GDP growth was just 1.8 percent, down from 2.2 percent the year before. Companies expect that their business potential, at least, will be limited by trade barriers or by restrictions on the free movement of workers.

¹ DIHK Survey: Initial Assessment of Brexit by Companies in Germany, June 2016

Situation and Outlook of German Companies for UK Business In percentages and net points



All companies affected

Companies' assessments hardly differ based on size, although companies with EUR 10-50 million in annual revenues are especially pessimistic about the development of business in the United Kingdom. However, the most pessimistic companies are those which import goods and services from the United Kingdom (net value of negative 35). These companies are worried about adverse changes in the supply chain and an increase in customs bureaucracy, resulting in higher costs. Exporting companies are just behind, with a net value of negative 30.

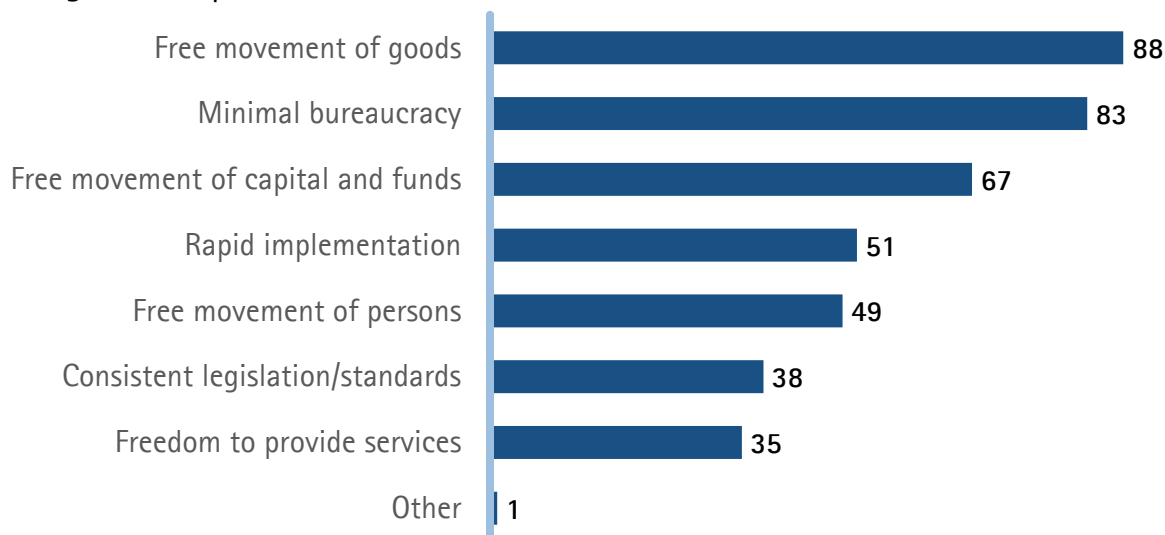
Priorities for the Brexit Negotiations

Prevent trade barriers!

At the top of the agenda for companies with regard to the upcoming Brexit talks, and for the negotiations of a trade agreement between the EU and the United Kingdom which are likely to follow is preserving the free movement of goods and avoiding an increase in customs bureaucracy. 88 percent of companies view the prevention of tariffs and import taxes as an important issue for the upcoming negotiations. Close behind, with 83 percent, is the challenge of minimizing bureaucratic red tape with regard to customs. After the UK withdraws from the EU, after all, companies would likely have to file formal customs declarations for imports and exports, as well as having to obtain export licenses for certain goods.

Priorities for the Brexit negotiations

Percentage of companies



Major fundamental freedoms of the internal market

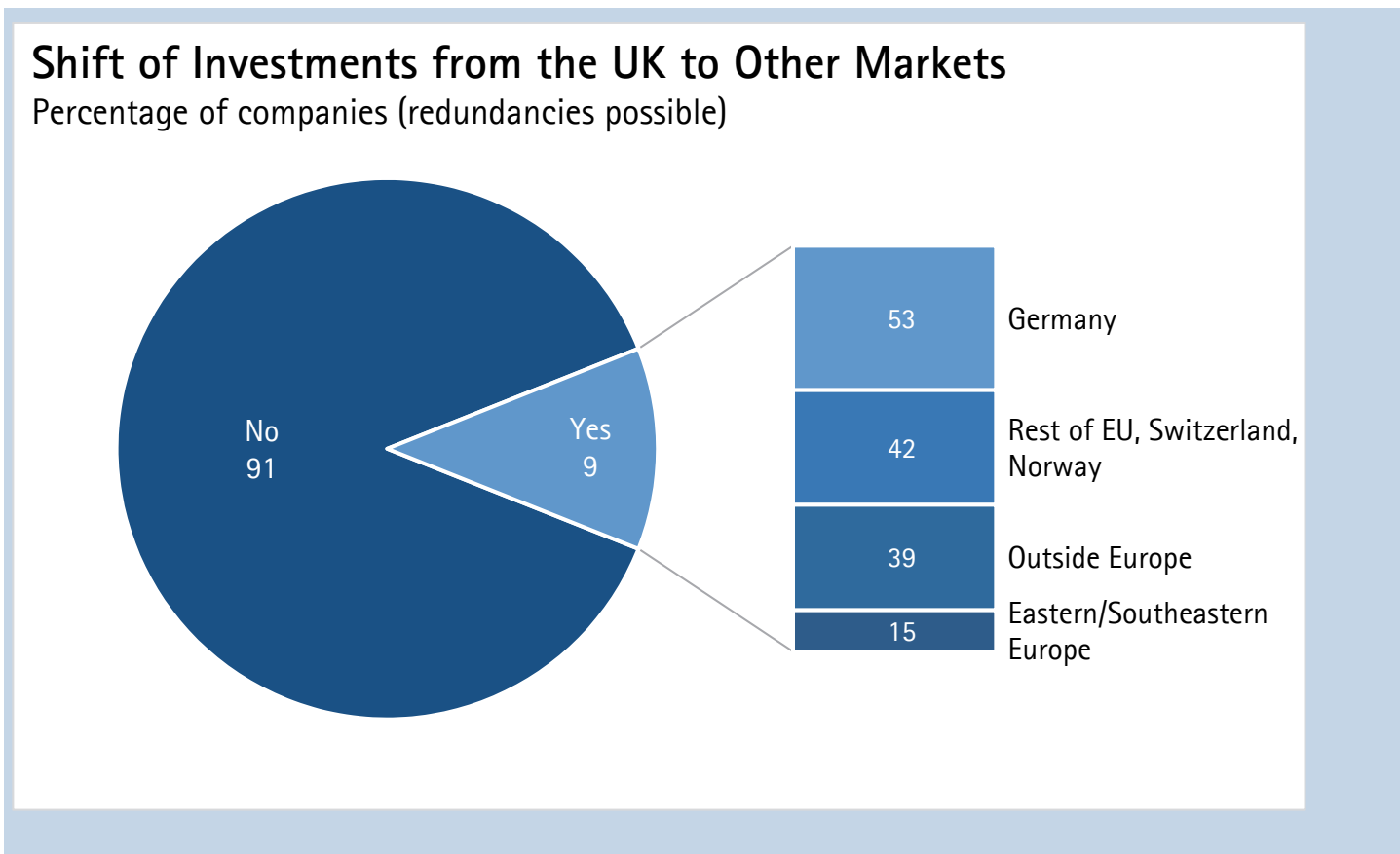
Following on companies' scale of priorities, with about half of respondents, is continuing to ensure free movement of persons and rapid implementation of Brexit so as to eliminate existing uncertainty. One third of companies cite the freedom to provide services and avoiding differences in legislation as important issues. But at the same time, companies are aware that the UK's withdrawal from the internal market will represent a severe setback and that cherry-picking concessions would hurt the internal market. Nevertheless, the challenges for future trade relations between the EU and the United Kingdom are great, especially since the UK is Germany's third-largest export market, with EUR 86 billion in exports. But the issues cited illustrate the most important aspects from the viewpoint of German companies.

Shift in Investments

Shift in investments

Almost one in every ten companies with investments in the United Kingdom is currently planning to shift to other markets because of the UK's withdrawal from the EU, even though the terms of the withdrawal are not yet known. This is a demonstration of how unsettled German companies are. In the near term, the weakened British Pound could compensate at least partially for a decline in investments. In

addition, the long-term risk of barriers to German exports can be mitigated by investing in British production sites.² But in the long run, a steep decrease in German investments in the United Kingdom seems highly likely.



A shift towards Germany and the EU

Companies planning to shift their investments because of Brexit have several options with regard to future target regions. Somewhat over one half of companies expect to redirect their investments towards Germany. As a result, the German economy may benefit from the shift in investments, which would mitigate the overall negative impact of Brexit at least somewhat. But other EU states would benefit as well, as companies attempt to preserve the advantages of the internal market. However, 39 percent of companies see investing outside of Europe as an option, including Eastern and Southeastern European countries which are not EU member states but offer other advantages, such as lower wages.

² DIHK Survey: Foreign Investments in the Industrial Sector, spring 2017

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