SMMT
DRIVING THE
MOTOR INDUSTRY

UK AUTOMOTIVE TRADE
REPORT 2023

OPEN ROADS

Driving Britain's global automotive trade

UK Automotive is on course to reclaim its position as a £100 billion-plus trading powerhouse by the end of 2023, a figure that Covid-19 cut by a quarter

CONTENTS

FOREWORD

The automotive industry's ability to navigate uncharted terrain remains undiminished: a global pandemic, war in Ukraine, prolonged supply chain shortages and the once-in-a-generation shift towards electrification – all in addition to Brexit, a cost-of-living crisis and soaring inflation. All were, or are, massive challenges that would test any industry, yet our sector has demonstrated its resilience and pathway to growth, growth firmly driven by global trade.

UK Automotive is on course to reclaim its position as a £100 billion-plus trading powerhouse by the end of 2023, a figure that Covid cut by a quarter. This underlines the significant role played by the sector in generating employment, fostering growth and acting as a significant contributor to the broader UK economy. Automotive represented nearly 12% of all Britain's manufactured goods in the first half of this year and almost one in eight UK-built exports. These include high value, cutting-edge vehicles shipped to all corners of the world from globally renowned brands, parts and components from companies synonymous with quality and innovation and, increasingly, new tech products designed to meet changing mobility needs.

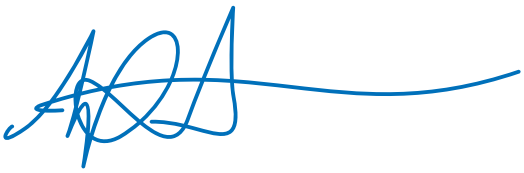
In this post-pandemic world, the UK remains a global leader in automotive production and exports, with an increasing number of cars, vans, buses, trucks, taxis, specialist and even off-highway vehicles transitioning towards zero emissions. With recent significant inward investment, the UK's expanding zero emission vehicle supply chain is not only adapting to change but working to become a global leader.

We have committed to net zero mobility, not just as a response to regulatory pressure or government commitment, but to provide a sustainable future for generations ahead. To achieve this ambition we must have free and fair trade with Europe and other established and emerging markets worldwide.

The EU is our largest trading partner – receiving almost 60% of UK passenger vehicle exports and supplying more than 71% of the cars we import. So finding a solution to prevent the imposition of tariffs on electric vehicles and batteries as set by the current EU-UK Trade and Cooperation Agreement rules of origin is our most pressing challenge. Failure to do so risks a £4.3 billion hit to the sector across Europe, which, in effect, will add a tax on the very vehicles needed for us to decarbonise road transport.

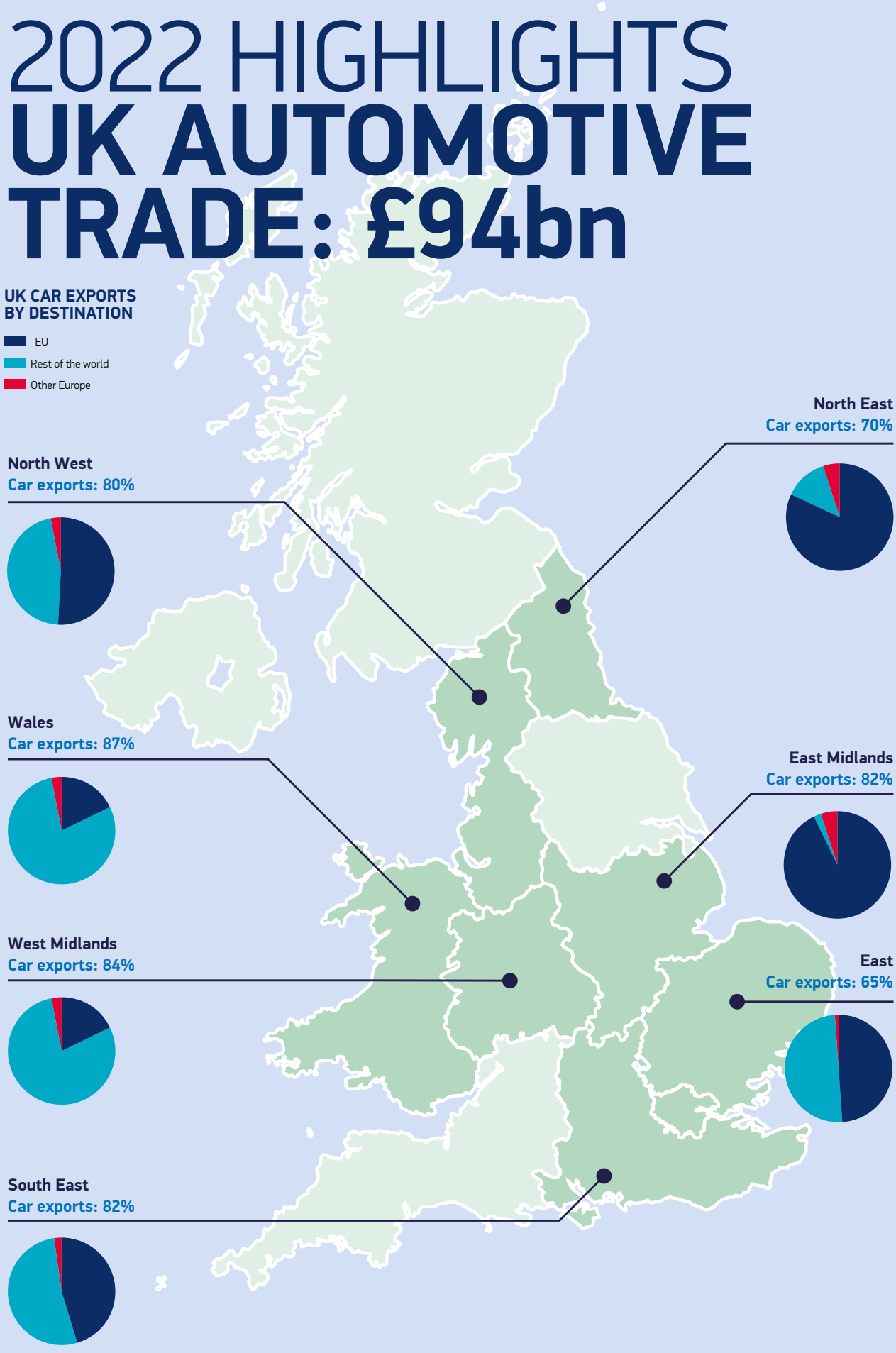
Safeguarding trade with the EU is critical but, as this report sets out, we must remain focused on trade around the world. This means addressing many challenges. Ensuring new and revised free trade agreements, especially with India, South Korea, Canada, Mexico and the Gulf states. Delivering enhanced market access and workable origin requirements for EVs, batteries and related components. Building on recent investment wins to develop a sustainable battery and critical mineral supply chain in Britain. Improving support for remanufacturing and recycling. Enhancing regulatory engagement with key trading partners so our small volume manufacturers remain competitive. And remaining alert to any adverse impacts from global trade tensions.

Solve that puzzle and the benefits are tremendous – jobs, growth and prosperity across the UK. Committing to free and fair trade is how we will spur investment, sustain competitiveness and deliver zero emission products that address the global challenge of climate change.



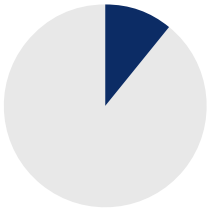
Mike Hawes Chief Executive
The Society of Motor Manufacturers and Traders (SMMT)

2022 HIGHLIGHTS
UK AUTOMOTIVE TRADE: £94bn



EXPORTS

£34.4 billion Value of exports



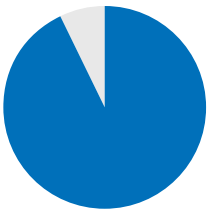
Automotive makes up 11.8% of all UK manufactured goods exports

TOP 10 CAR EXPORT DESTINATIONS 2022

EU	57.6%
USA	13.3%
China	8.7%
Japan	2.9%
South Korea	2.0%
Australia	1.9%
Turkey	1.4%
Canada	1.3%
Mexico	0.6%
UAE	0.4%
Other	9.9%

IMPORTS

£59.4 billion Value of imports



71% of imported cars to the UK come from the EU

TOP 9 CAR IMPORT ORIGINS 2022

EU	71.3%
China	9.2%
South Korea	5.8%
Japan	5.8%
Turkey	3.6%
Mexico	1.4%
South Africa	1.3%
USA	0.9%
Morocco	0.7%

30%

Electrified vehicle exports up almost 30% in the first half of 2023 (vs 2019)

97%

Almost 97% of new battery electric vehicle (BEV) registrations were imported vehicles in the first half of 2023

EV TRADE

Exports of EVs to EU **£5.6bn**

Imports of EVs from EU **£9.7bn**

EV RULES OF ORIGIN IMPACT

£3,400

New figures reveal tariff threat to EU-made Electric Vehicles could result in a £3,400 average price hike if unworkable rules of origin are implemented in January

£3,600

10% tariffs would also add £3,600 to cost of British-built EVs sold in Europe, with conventional ICE models unaffected on both sides.

RECOMMENDATIONS FOR GOVERNMENT AND INDUSTRY

01 TCA ORIGIN REQUIREMENTS FOR BATTERIES

The UK and the EU should agree urgently to delay the introduction of tougher battery rules for three years.

02 ACHIEVE FTAs FIT FOR EVs

Ensure new and revised FTAs deliver enhanced market access and workable origin requirements for EVs, batteries and related components.

03 INCREASE UK VALUE-ADDED

Devise a national advanced manufacturing plan to attract additional investment throughout the battery supply chain and ensure the automotive sector can fully benefit from all UK FTAs.

04 CRITICAL MINERALS NETWORK

Agree new critical minerals partnerships with resource-rich countries and major EV markets, seeking both soft and binding commitments to encourage investment and enhance supply chain reliability.

05 INTERNATIONAL CIRCULAR ECONOMY

Support the circular economy by streamlining the tariff suspension mechanism and devise a tailor-made strategy to reduce costs of international sourcing of materials needed by remanufacturers and recycling companies.

06 ENGAGE WITH CHINA

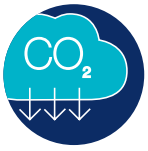
Monitor potential adverse impacts on the UK automotive industry from the EU's investigation into Chinese EV subsidies. UK manufacturers should support engagement with China by providing meaningful insights into market challenges. Enhanced bilateral dialogue could help address market access barriers.

07 OPEN ROADS TO INDIA

Step-up engagement to reach a balanced, commercially meaningful agreement with India providing additional market access across all automotive products on the basis of workable origin requirements.

08 TRADE CONTINUITY WITH SOUTH KOREA

Launch, negotiate, finalise and bring into effect a modernised UK-South Korea Free Trade Agreement before the expiry of the extended EU cumulation clause.



09 COOPERATE TO ADDRESS CARBON LEAKAGE

With the UK and several other countries already implementing Emission Trading Schemes and considering the implementation of CBAMs similar to the EU's, European automotive businesses might benefit greatly from the recognition of equivalent regulatory regimes and the reduction of administrative burdens and additional costs in movements of covered products between them.

10 DEVELOP A SUSTAINABLE SUPPLY CHAIN

EU regulations on corporate sustainability are likely to set a new global benchmark. It is essential for automotive businesses operating in the UK and in the broader European region to familiarise with new and upcoming obligations and put in place the necessary compliance mechanisms.

11 TRADE WITH THE GULF

Finalising an ambitious new FTA with GCC countries could open commercially meaningful opportunities if the parties agree on enhanced market access commitments.

12 BUILD ON THE ATLANTIC DECLARATION

Finalise negotiations of a US-UK critical mineral partnership to improve market access in the US for critical minerals extracted, refined or recycled in the UK.

13 REFORGE TRADE TIES IN NORTH AMERICA

Conclude the negotiation of upgraded FTAs with Mexico and Canada and secure an extension of existing EU cumulation clauses to ensure trade continuity until the new agreements take effect.

14 GO TO BAT FOR ICONIC BRITISH BRANDS

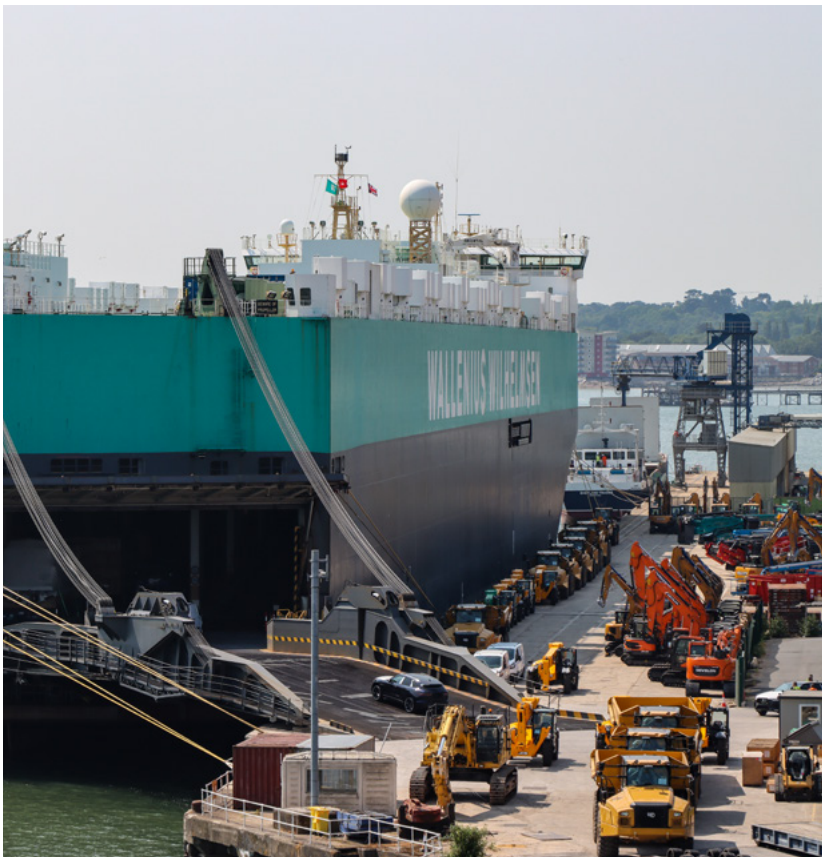
Enhance regulatory engagement with key trading partners to seek additional flexibilities for SVMs and mitigate against impacts of overburdensome regulatory and behind-the-border barriers.

UK AUTOMOTIVE TRADE SNAPSHOT

→ **UK Automotive delivered £94 billion in trade in 2022, with the sector eyeing the possibility of regaining its status as a £100 billion plus trade hub by the end of 2023.**

→ **The Automotive sector remains pivotal to the UK's economy, representing 11.8% of all exports of UK manufactured goods in the first six months of 2023 and road vehicles topping the list of the country's most imported commodities.**

→ **The industry remains open to the world, with the EU consolidating its position as the sector's largest trading partner receiving almost 60% of UK car exports and supplying more than 71% of imported new cars.**



TOTAL AUTOMOTIVE TRADE

Despite being severely tested by years of extraordinary economic turbulence and systemic disruptions, the UK automotive sector remains a multi-billion pound trade hub, demonstrated by its ability to deliver £94 billion in trade value at the end of 2022 – a year marred by the fall-out of multiple global and regional crises.

Most importantly, with imports and exports of finished vehicles, parts and components worth some £101 billion in trade in the first half of 2023 (on a rolling year basis), the UK automotive industry seems fully on track to regain its pre-pandemic role as a £100 billion plus trade generator by the end of the year.

UK Automotive aspiring to reclaim its position as one of Britain's most valued trade hubs, just three years from the Covid-19 pandemic, is a testament to the strong fundamentals of the sector. This includes the ability of domestic manufacturers and importers to adjust their business operations in the face of adverse conditions, ongoing supply chain issues and the determination to remain an open market despite growing international competition.

During the 2020-2022 period, unexpected challenges have hindered the industry's ability to recover quickly after the pandemic, with automotive export values facing the most significant impacts.

The pandemic and the consequential lockdowns resulted in widespread market closure causing production to halt in the UK alongside other major automotive hubs. Despite the gradual shift from lockdown to a managed risk approach, thanks to the vaccination programme rollout worldwide, the expectations of a strong rebound in sales and production were frustrated by supply shortages – most notably of semiconductors and other raw materials, as well as systemic staff shortages.

Furthermore, the introduction of new trade barriers in exchanges between the UK and EU following the UK's exit from the European Single Market and Customs Union in 2021 has impacted this highly integrated automotive supply chain.

More recently, the full-scale invasion of Ukraine launched by Russia in February 2022 further exacerbated production challenges, as exemplified by Ukrainian wire harness suppliers forced to stop manufacturing operations overnight and major shortages of Ukrainian neon gas – a crucial commodity in the production of chips. The impact of sanctions adopted in response to the aggression, coupled with skyrocketing prices for energy and key manufacturing inputs, such as palladium and aluminium, fuelled the most significant inflationary crisis in decades, with the UK among the hardest hit.

These challenges caused major disruptions to the UK automotive industry's cost-sensitive business model and could have resulted in the systemic marginalisation of the sector as a significant contributor to the UK's trade balance sheet. While last year's overall trade performance was driven by the strong rebound in automotive import values, exports struggled to recover to pre-pandemic levels.

However, even in 2022, when inflationary pressure and the unique market conditions pushed exports of basic precious metals to more than double in one year, UK automotive exports covered almost 10% of all exported manufactured goods. In the first half of 2023, the share of UK automotive exports has increased to 11.8%, bringing the industry a step closer to the 13% threshold recorded before the pandemic outbreak.

Chart 1 **Total automotive trade value (Motor vehicles, trailers & semi-trailers, parts & components)**

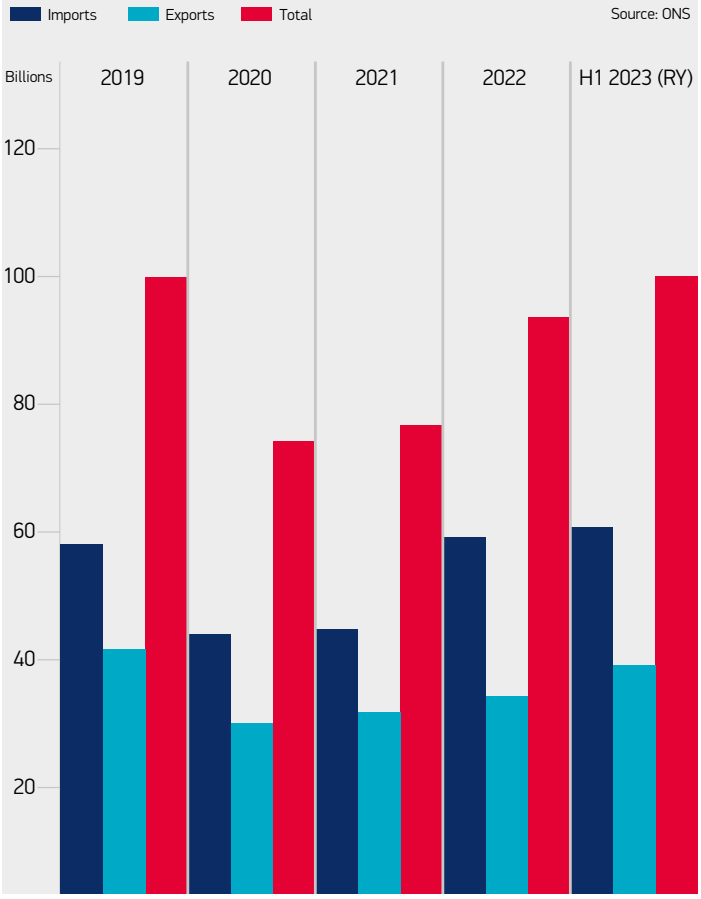


Chart 2 **Automotive share of all UK manufactured good exports (%)**

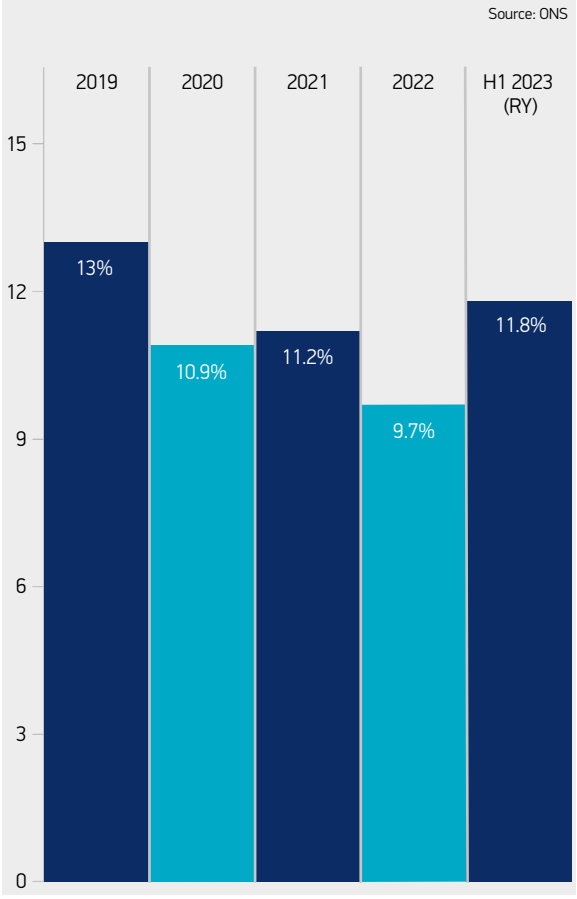
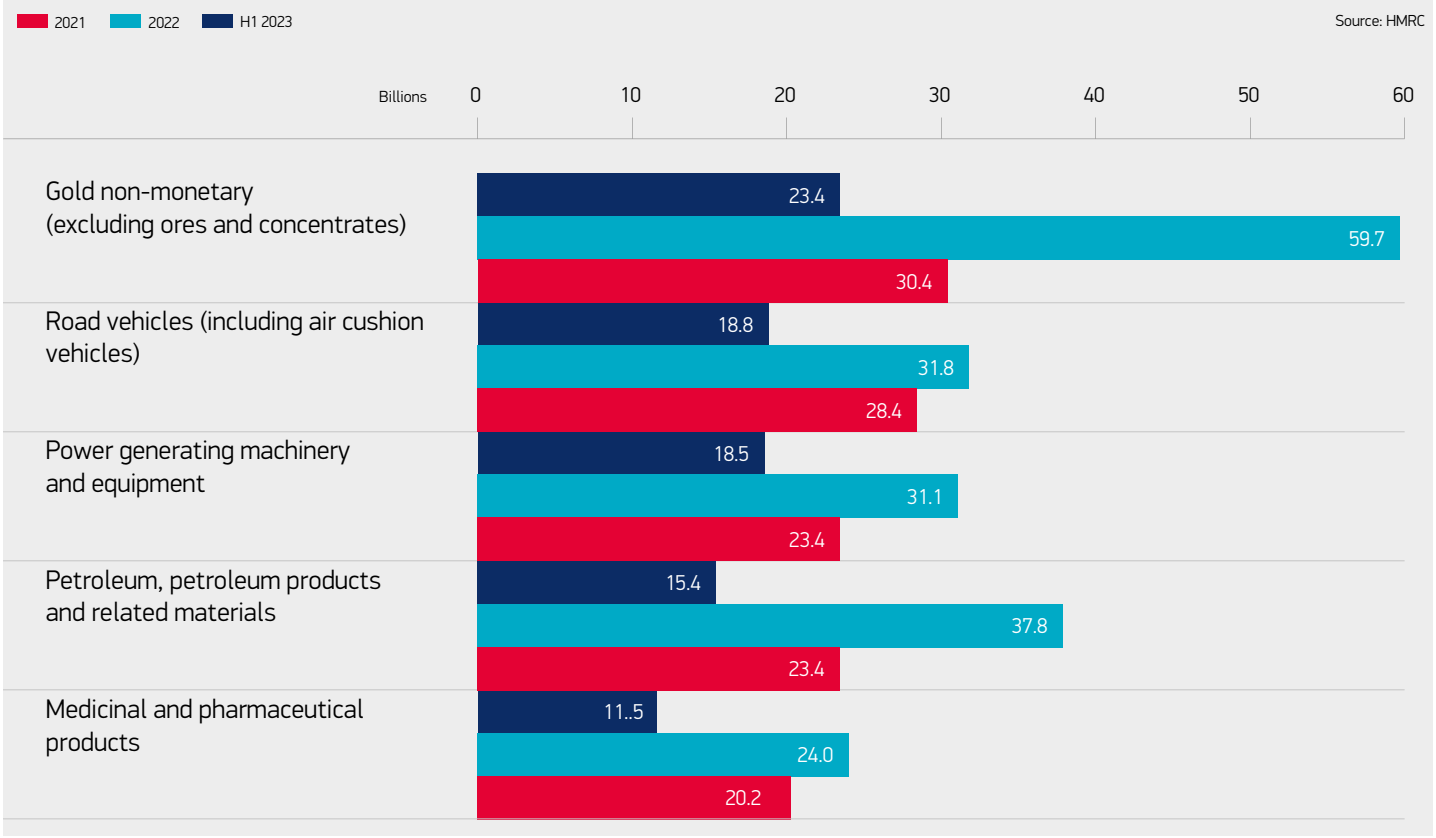


Chart 3 **TOP 5 UK Goods exports Standard international trade classification (SITC)**



EXPORTS OF FINISHED VEHICLES

After three years of extraordinary market turbulence, road vehicles are slowly regaining their traditional position as the UK's most exported commodity.

In 2022, the energy crisis and inflationary pressure on energy products led to a boom in export values of petroleum and related products, while the exceptional performance of gold exports appears to be a response from global investors to the geopolitical and economic crisis that unfolded after the invasion of Ukraine. Despite two years of steady growth in export values, it is no surprise that road vehicles became the UK's third most exported good at the end of 2022, with a value of £31.8 billion.

As markets adjust to the new economic environment, exports of gold are progressively normalising and there are signs that motor vehicle exports have regained momentum in the first half of 2023, with a value of more than £18.8 billion, just below gold exports, and the possibility to return to pre-pandemic levels by the end of the year, if current trends are maintained.

Chart 4 **UK vehicle production (rolling year basis)**

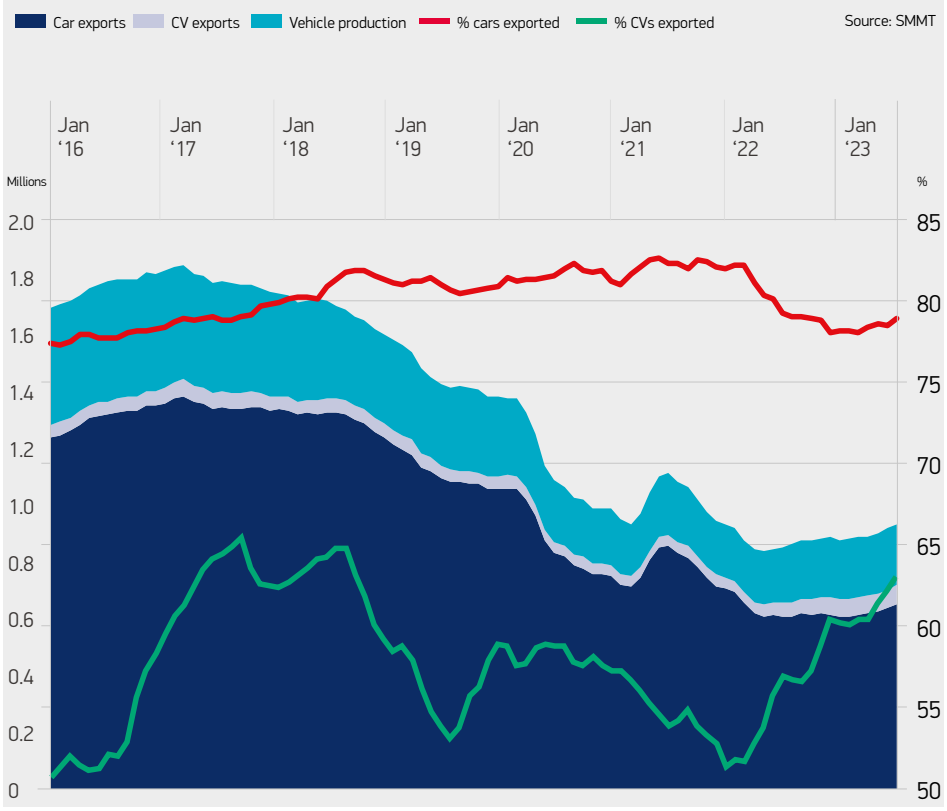


Chart 5 **Top 10 car export destination by volume**

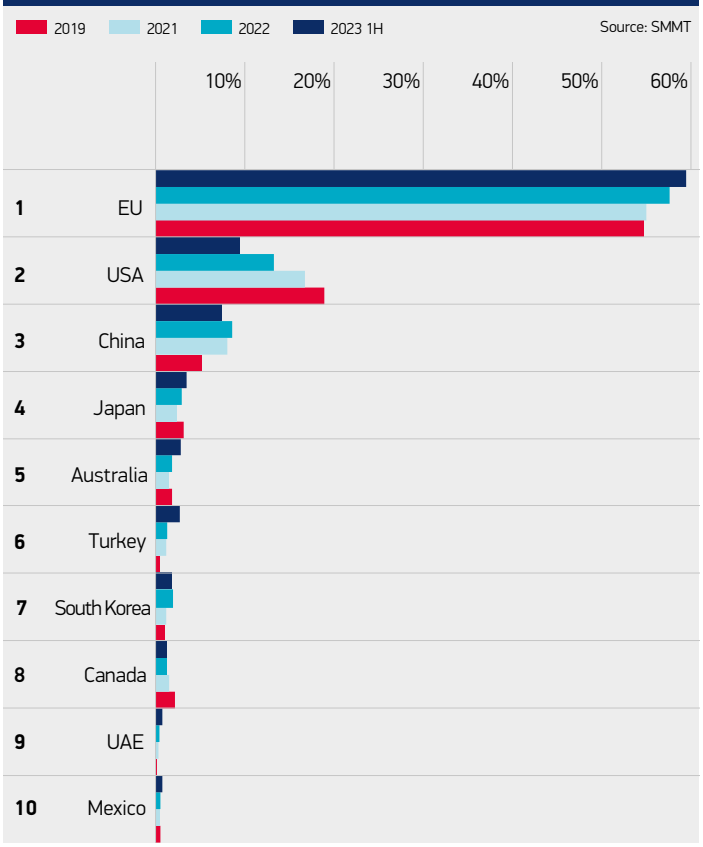
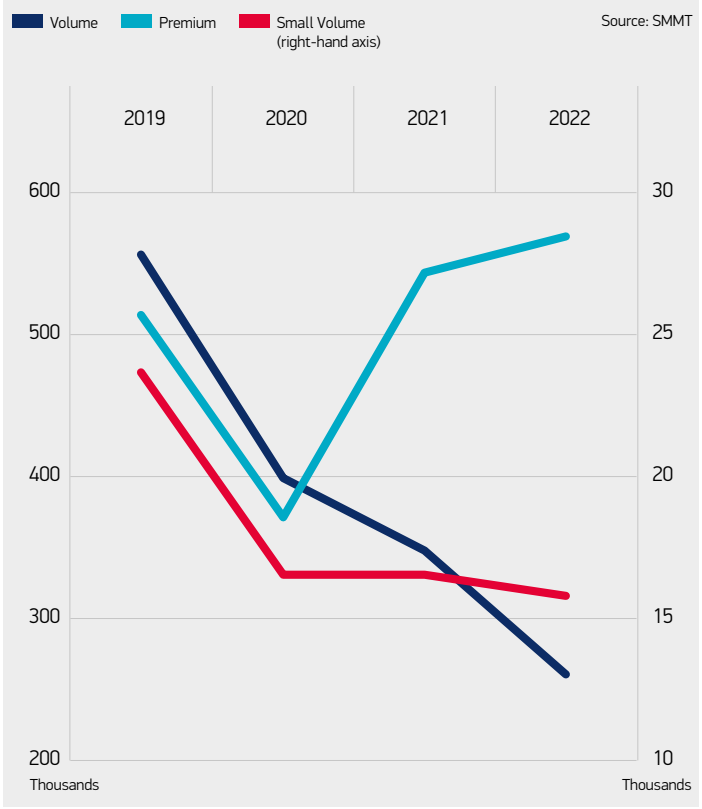


Chart 6 **UK car exports by type (volume)**



Although values are on course to regain their pre-pandemic level, export volumes remain far below the one million unit threshold recorded, for the last time, in April 2020.

At the end of 2022, just over 600,000 cars were shipped globally from the UK. In the first half of 2023, the industry had reported a 7% increase to 650,000 exported units on a rolling year basis. Despite the latest positive performance, full recovery remains elusive, with export volumes in 2023 (on a rolling year basis) remaining -38.4% below 2019 levels. Furthermore, the loss in export volumes since 2020 was not compensated by additional sales for the domestic market, as the sector remains firmly export-oriented, with almost eight out of 10 cars produced in the UK sold to customers overseas.

Supply chain disruptions, systemic shortages and broader inflationary impacts can partially explain the disconnect between export values and volumes. However, the major difference in growth rates – with export values increasing by 34% and export volumes up by just 7% in the first half of 2023 – points to a structural change following the loss of Honda and Vauxhall Astra models and the ensuing reduction in exports from volume manufactures. Manufacturers are likely seeking higher profitability and are adjusting to the different cost structures of lower emission vehicles, with vehicle assemblers incorporating high-value batteries – including associated parts and critical minerals – and advanced technologies into their finished products.

The world's four largest economies have been consistently ranked as the top export destinations for UK-built passenger cars. Although the industry exports to all corners of the world, the four biggest markets – namely the EU, the US, China and Japan – have a cumulative share of almost 80% of all UK car exports.

Among the big four, the EU is consolidating its dominant position, with 59.5% of all exported UK cars shipped to the bloc in the first half of the year (versus 57.6% in 2022 and 54.8% in 2019). Honda's decision to discontinue production in the UK resulted in a major decline in exports to the US and the progressive growth in the relative weight of exports destined for the EU and other markets, with the relative weight of export volumes to the US falling from 18.9% in 2019 to 9.5% in the first half of 2023. With the exception of the US and Canada, all other export destinations in the top 10 recorded an increase in their relative weight compared to 2019. China (7.4%), Japan (3.5%), Australia (2.9%), Turkey (2.7%), South Korea (1.8%) and Canada (1.3%) maintained their spots in the top 10, while the UAE (0.8%) and Mexico (0.8%) are notable new entries, with Switzerland and South Africa dropping out of the list in the first half of the year.

The decline in export units is driven mainly by the reduction in exports of volume manufacturers, noting the above structural issues. Premium vehicle manufacturers recorded a slight dip, while exports from small volume manufacturers (SVMs), traditionally high-value luxury and sports vehicles, have fully recovered since 2021. These changes contributed to the diverging patterns between export values and volumes.

The UK automotive industry is a vital part of the UK economy, with a domestic presence in regions across the country and an export footprint spanning the globe. All UK regions hosting car assembly operations are strongly export-oriented. The percentage of cars produced for exports in each individual region ranges from a minimum of 65% in the East of England to peaks of 84% in the West Midlands and 87% in Wales.

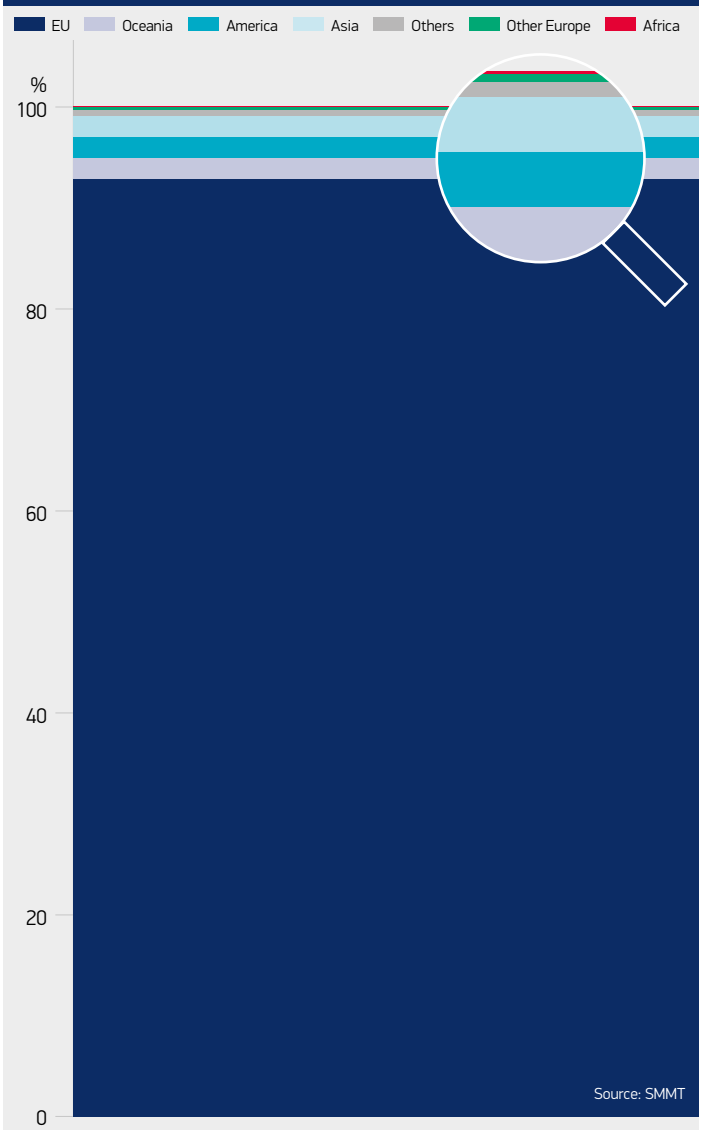
An exception to the sluggish export volume trend is the strong rebound in shipments of British-built commercial vehicles (CVs). By the end of 2022, the UK was exporting almost 40% more CVs than in 2019, with more than six out of 10 destined for overseas markets and more than 66,000 CVs exported in the first half of 2023 (on a rolling year basis). The UK CV industry benefits from the rapid expansion of delivery services during and after the pandemic, with domestic CV manufacturers well positioned to capture market growth. However, with more than 90% of CV exports destined for the EU, this market segment remains highly dependent on single market demand cycles. The diversification of the CV export portfolio might represent an opportunity to consolidate the sector's export outlook and create economies of scale.

The UK automotive sector remains a multi-billion pound trade hub, demonstrated by its ability to deliver £94 billion in trade value at the end of 2022

Table 1 **Share of car production for exports from each region**

North East (England)	70%
North West (England)	80%
Yorkshire and The Humber (England)	n/a
East Midlands (England)	82%
West Midlands (England)	84%
East of England	65%
London	n/a
South East (England)	82%
South West (England)	n/a
Wales	87%
Scotland	n/a

Chart 7 **CV exports - destinations (share all exports) 2023 1H**



IMPORTS OF FINISHED VEHICLES

The UK remains an open market, with imported cars covering more than 90% of all new car registrations in the first half of 2023 and volumes increasing to above 1.6 million units on a rolling year basis. According to HMRC, road vehicles consistently top the list of the most imported commodities by value, with inbound shipments worth more than £58.5 billion last year, ahead of petroleum products and gas.

The UK receives new cars from nine different trading partners, with the EU being our largest supplier covering 71.3% of all imports. Chinese-built cars have seen their market share increase from less than 1% in 2019 to account for 9.2% of all imports in the first half of 2023 – a consequence of the rising electrification of the UK's new car market. Other Asian nations are also performing well in the UK, notably South Korea and Japan rounding out the top four importers.

The UK light commercial vehicle (LCV) market is also dominated by imports, with their share consistently exceeding a 90% market share since 2016. Imported LCVs are predominantly sourced from the EU (63.7%), however, Turkey covers 23.2% of all LCV imports and remains a major van supplier with close links to both the UK supply chain and British customers.

Chart 8 **UK new car registrations – imports volume and share**

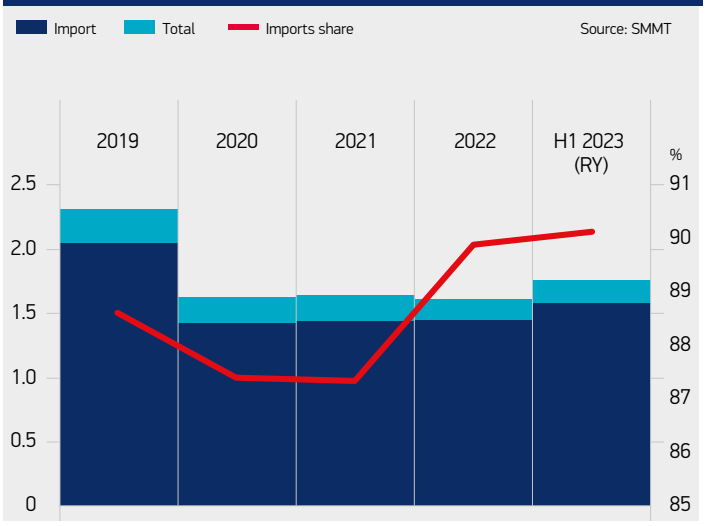


Chart 9 **Top 9 car imports origin (share of total)**

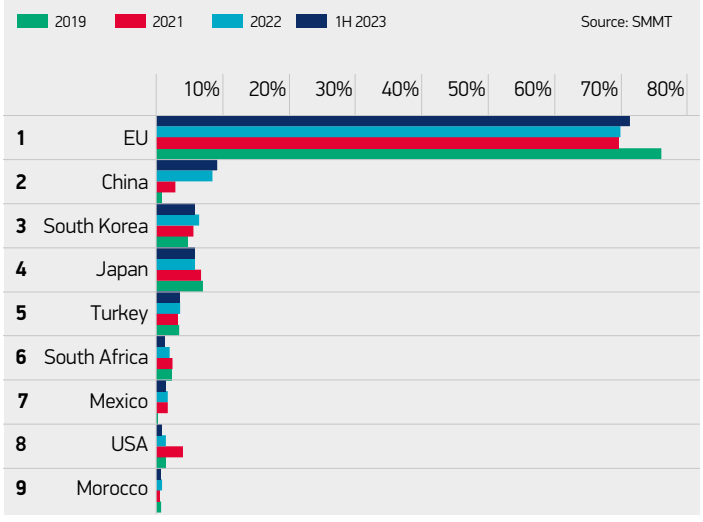


Chart10 **UK new LCV registrations – imports volume and share**

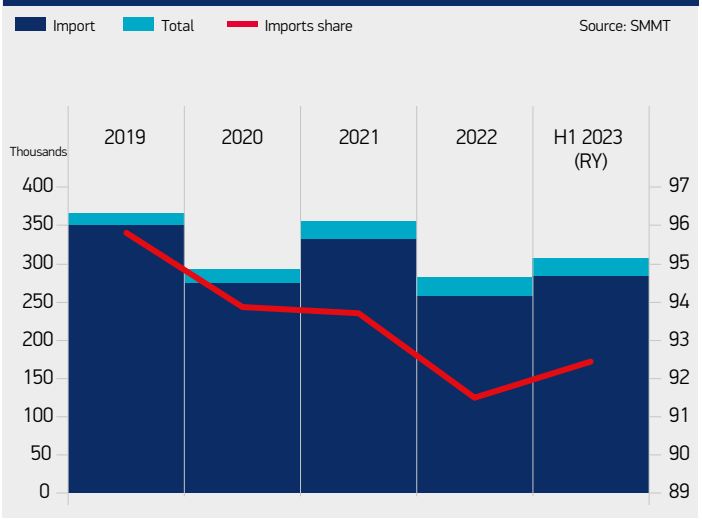
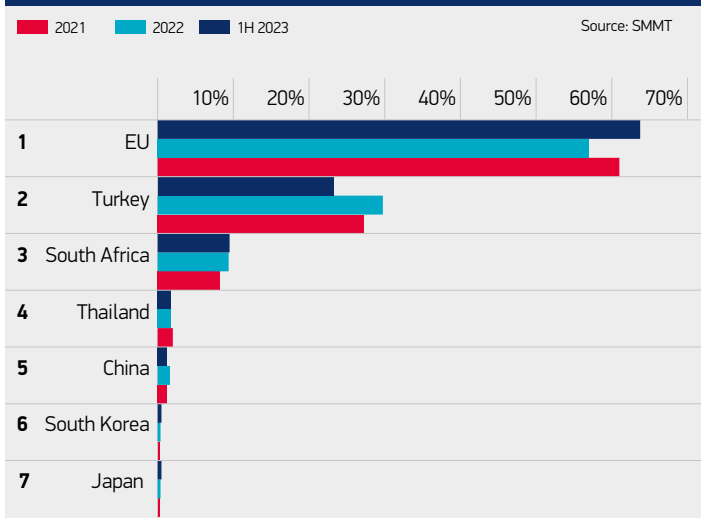
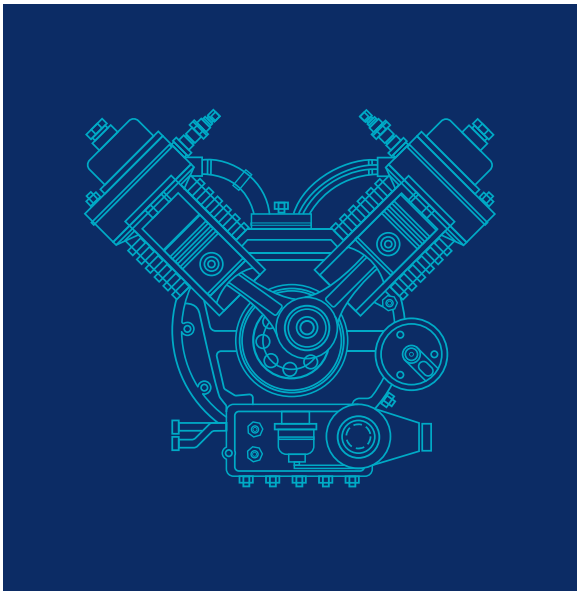


Chart11 **Top 7 LCV imports origin (share of total)**



TRADE IN ENGINES AND PARTS

In 2022, the cumulative value of trade in typical parts and engines amounted to more than £17.2 billion.



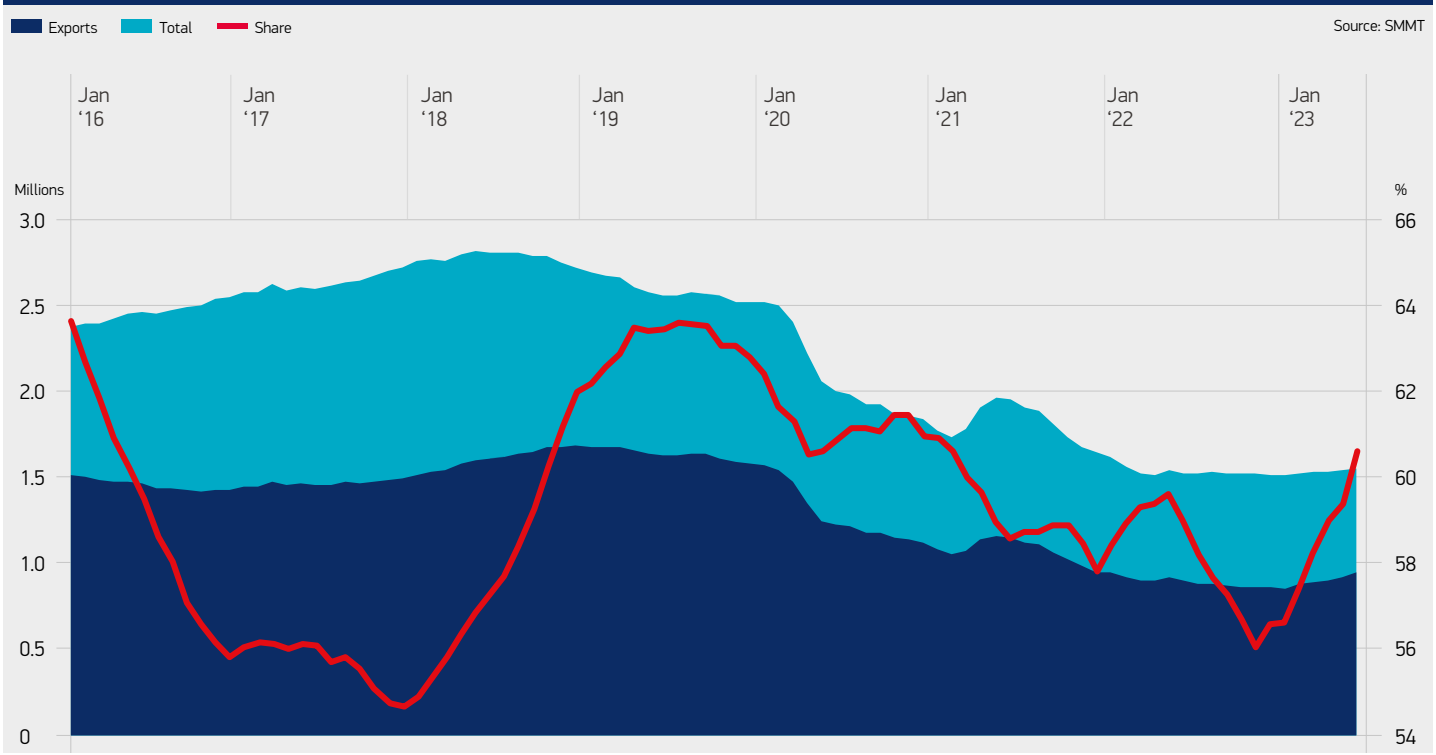
Last year, the UK turned out more than 1.6 million engines, with 57.8% of all units exported overseas. Engine production and export volumes have flatlined in the first half of 2023, remaining below the traditional pre-pandemic level of more than 2 million units manufactured on a rolling year basis.

Engine exports remain a significant contributor to the UK's economy, with shipments overseas valued at more than £2.1 billion in 2022. However, following years of decline, engine imports are accelerating at a faster pace than exports, with inbound shipments worth more than £1 billion in 2022 – driven by a 45.5% annual increase in imports from the EU.

Similar to engines, trade in components has not yet fully recovered. In 2022, imports and exports of typical parts and accessories remained below pre-pandemic levels, despite a 7.5% annual increase, to a total value of more than £14 billion.

The UK supply chain remains deeply integrated with its closest neighbours, as the EU maintained its position as the UK automotive industry's dominant supplier and main export destination for British parts. Trade with the EU regained momentum in 2022 after losing ground compared with trade to the rest of the world in 2021. However, exports from the UK to non-EU markets were already above pre-pandemic levels in 2022, and trade in parts with the rest of the world is on course to fully recover by the end of 2023, while a return to 2019 values in trade with the EU is unlikely.

Chart 12 **UK engine production (rolling year basis)**



Engine exports remain a significant contributor to the UK's economy, with shipments overseas valued more than £2.1 billion in 2022

Chart 13 **Total engine trade (value)**

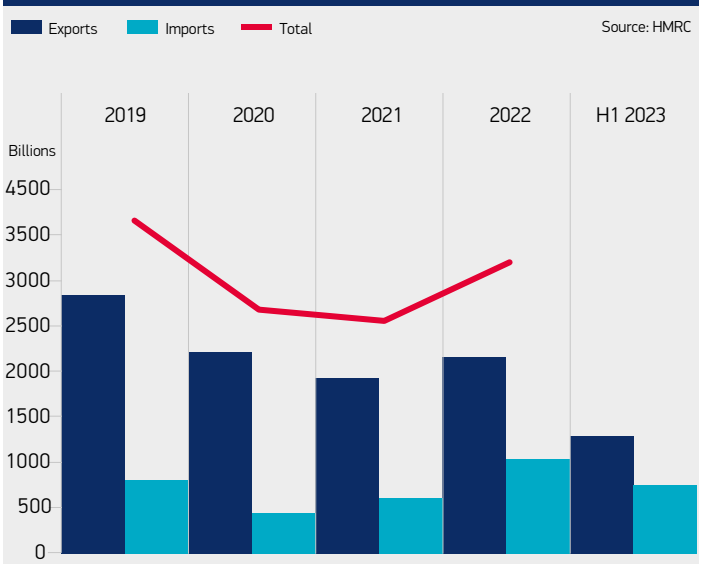


Chart 14 **Total trade of parts and components (value)**

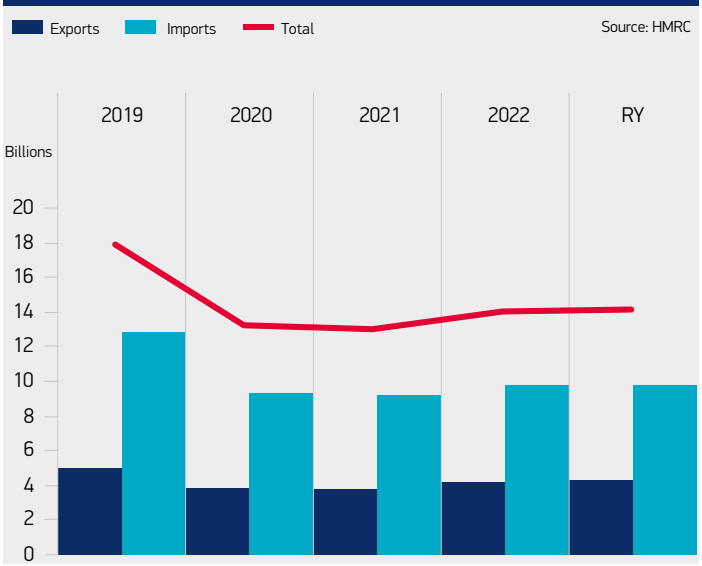
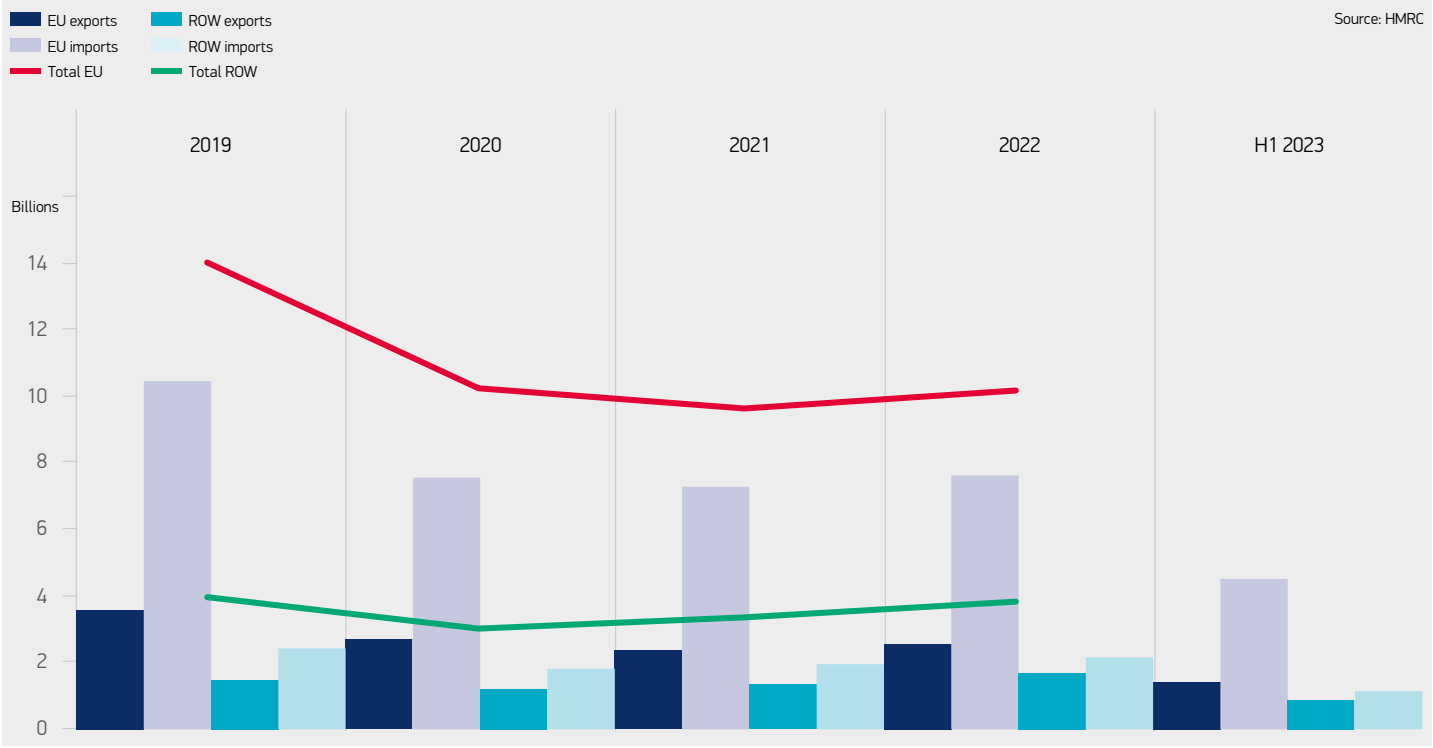


Chart 15 **Trade in parts - EU vs ROW (Value)**



EV FOCUS: FUTUREPROOFING UK FTAs

- → Trade in electrified vehicles (EVs) drive the sector's recovery, with exports of battery electric and hybrid vehicles already 30% above pre-pandemic levels. Imports of EVs from the EU and the rest of the world are crucial to support the UK's environmental ambitions.
- → The EU-UK TCA has created an enabling environment, with the value of bilateral EV trade growing more than 104% in three years, from £7.4 billion at the end of 2020 to £15.3 billion last year. However, the phase-in of unworkable origin requirements for batteries in 2024 risks derailing regional EV trade, with a potential tariff bill of £4.3 billion.
- → A three-year delay of the TCA battery origin requirements, the modernisation of continuity agreements, the negotiation of new FTAs setting realistic content requirements and additional investment throughout the battery supply chain are crucial to scale up international EV trade.

TRADE IN EVs

As supply chain bottlenecks ease, global trade should fuel growth in UK automotive production, boosting sales of both British-made and imported automotive products, and encouraging the transition to low-emission technologies by building economies of scale.

However, new international trade leads can be hard to find amid new and old barriers, with increasingly complex geopolitical, environmental and industrial policies.

In this context, trade in EVs represents a bright spot.

While the industry has faced a multiple-year decline in overall production and export volumes, the number of exported hybrid and fully electric passenger cars has steadily increased. After a minor decline in 2020 following the pandemic shock, by the end of 2021 exports in UK electrified vehicles (EVs) had already fully recovered. As EV outbound shipments recorded almost a 30% increase in the first half of 2023 compared with 2019 figures, it is increasingly clear that the future prosperity of the export-led UK automotive sector depends on the industry's ability to capture EV market growth abroad.

In parallel, with almost 97% of new battery electric vehicle (BEV) registrations being of foreign origin in the first half of 2023, imports are indispensable to achieve the UK government's commitment to a 100% reduction of greenhouse gas emissions by 2050 compared with 1990 levels (so-called Net Zero).

Almost half of all new BEVs registered in the UK are built in the EU, while Chinese-made BEVs have rapidly gained ground in the last four years, with the associated market share jumping from less than 2% in 2019 to 33.4% in the first half of the year. Notably, the boom in BEV imports from China has resulted from a successful export strategy of both homegrown and non-Chinese brands, with all Tesla models currently being delivered from Chinese factories and the dramatic drop of imports from the US from almost 35% before the pandemic to virtually zero since 2021.

Chart 16 **UK 'electrified' car production for export**

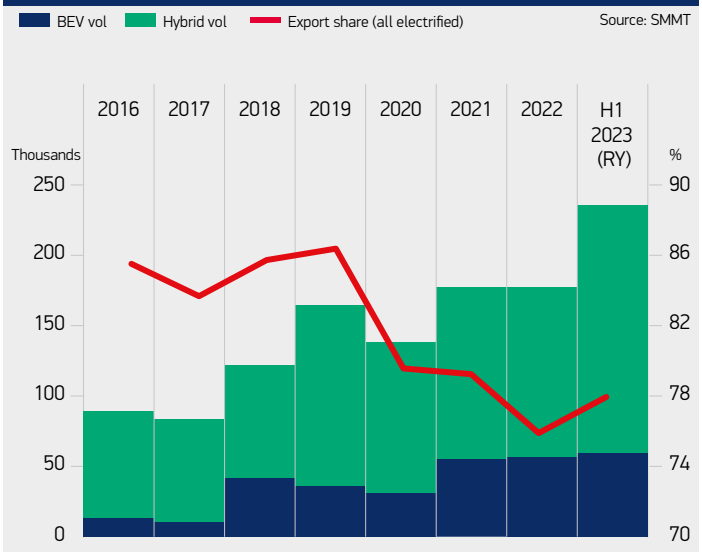
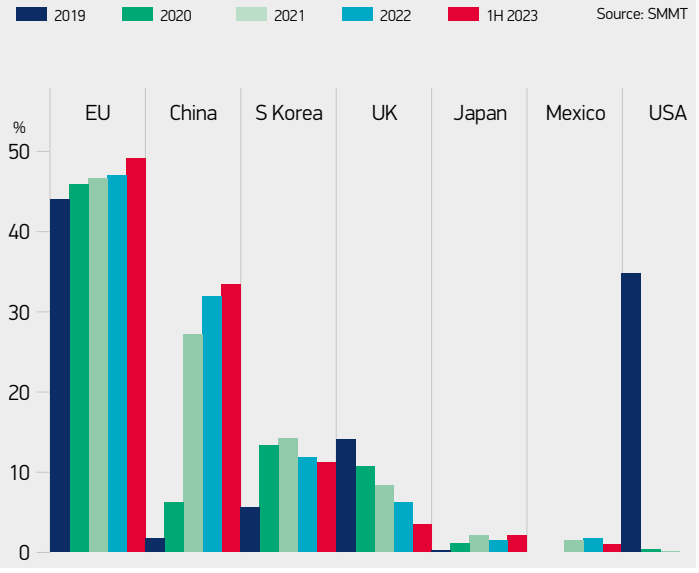


Chart 17 **UK BEV new car market by country of origin**



EVs UNDER THE TCA

An end-to-end EV trade and investment policy must deliver on all aspects of EV development, production and marketing, with the reduction of costs in trade of alternatively-fuelled vehicles and associated technologies being one of the industry's top priorities.

As hopes of multilateral trade liberalisation remain at a permanent standstill due to the systemic crisis at the World Trade Organisation, the reduction of EV tariff burdens depends largely on the ability of individual governments to conclude modern free trade agreements (FTAs).

In this regard, FTAs offer discounted tariff rates or full liberalisation only to products that comply with specific origin criteria. However, for decades, FTAs between the UK and its preferential trading partners delivered major opportunities for internal combustion engine (ICE) vehicles and associated technologies, while setting overambitious origin rules for EVs, battery packs and related components.

The conclusion of the Trade and Cooperation Agreement (TCA) between the EU and the UK was the first example of a European FTA providing a tangible opportunity to avoid tariffs on bilateral trade of EVs.

Taking into account the lack of a sufficiently developed Anglo-European supply chain for batteries and EVs, the TCA set exceptionally liberal rules on battery packs and finished vehicles on a temporary basis. Until the end of 2023, European battery manufacturers can enter the production process at the point of assembling imported battery cells and modules and the resulting products could still qualify under the provisional TCA rules. As batteries represent a significant percentage of the value of an EV, incorporating an originating battery pack usually allows the finished vehicle to meet its own origin requirement and avoid tariffs.

Although it is difficult to isolate the impacts of the TCA from other factors, the fact that bilateral trade in EVs has grown since the introduction of the TCA while trade in ICE has significantly declined compared with pre-Covid-19 and pre-Brexit levels testifies that the agreement has been a successful EV-trade enabler in the face of unprecedented challenges.

Imports of BEVs produced in Germany have performed particularly well following the introduction of the TCA, representing more than 57% of all EU BEV imports into the UK in the first half of 2023, followed by French-built BEVs on 12%.

However, with the expectation of a significant acceleration in investment throughout the European e-mobility supply chain, the parties also agreed to phase in more stringent rules on finished EVs, battery packs and battery parts in 2024 and in 2027.

While a reasonable 5% increase in regional content was agreed on EVs, 2024 rules for batteries can be met only through localising production of battery packs, modules, cells, cathodes, anodes as well as high-value cathode active materials in the European region. Despite battery investment picking up pace rapidly, major gaps in regional manufacturing capabilities remain, while skyrocketing prices for critical raw materials extracted and processed outside of the European region do not allow to meet alternative, equally demanding value-added requirements tolerating just 40% of the final value of a battery to be non-originating materials.

Should battery packs fail to qualify, the consequences for bilateral EV trade would be significant. As OEMs would need to deduct the value of a non-originating battery from the factory price of the finished vehicle, EU and UK EV manufacturers would likely fall short of their own origin

Chart 18 **Car exports to the EU - EV vs ICE**

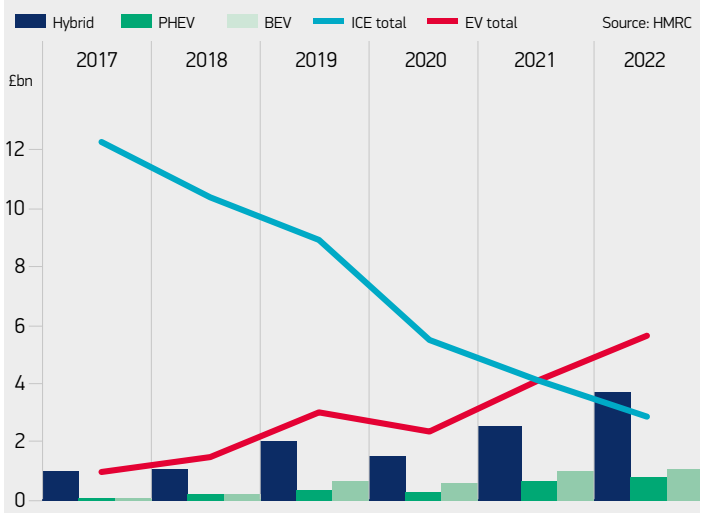


Chart 19 **Car imports from the EU - EV vs ICE**

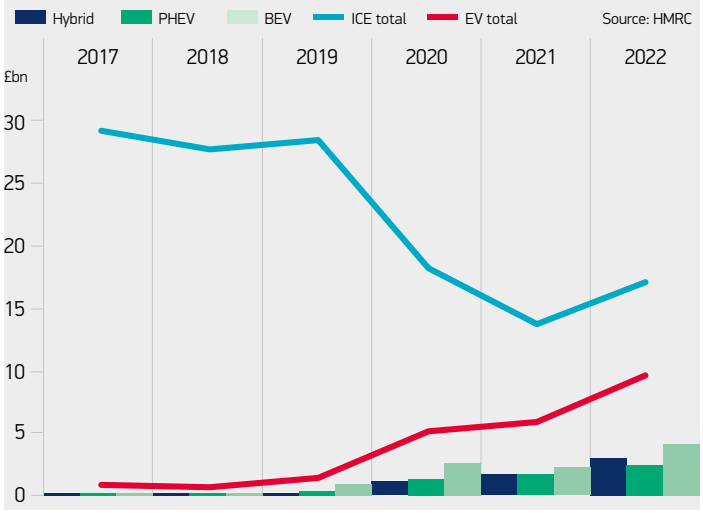


Chart 20 **Share of UK BEV registrations sourced from the EU - by top 10 countries (2022)**

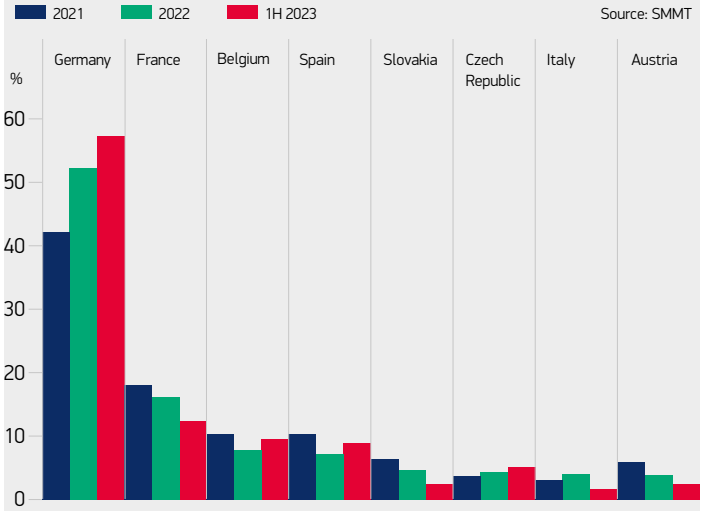
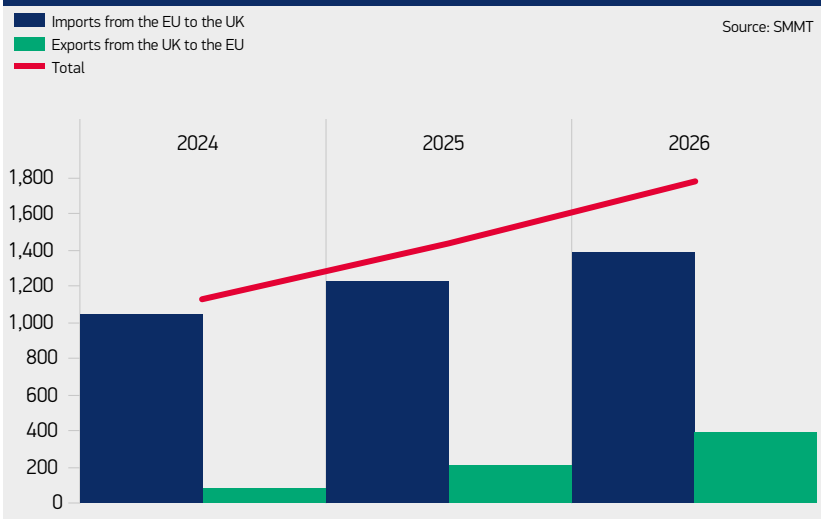


Table 2 **TCA Rules of origin for EVs, Batteries and Related components**

	1 Jan. 2021 – 31 Dec. 2023	1 Jan. 2024 – 31 Dec. 2026	2027 onwards
BEVs, PHEVs, HEVs (Passenger Cars, Commercial Vehicles, Buses)	60% Max Non-Originating Material (MaxNOM) / 40% Regional Value Content (RVC)	55% MaxNOM / 45% RVC	45% MaxNOM / 55% RVC and BEVs/PHEVs battery pack must originate in the UK/EU
Battery packs (PCs, CVs, buses)	- 70% MaxNOM – 30% RVC; or - CTSH; or - Assembly from non-originating battery cells or modules	- CTH (except from non-originating active cathode materials); or - 40% MaxNOM / 60% RVC	- CTH (except from non-originating active cathode materials); or - 30% MaxNOM / 70% RVC
Cells, Modules, parts	- CTH; or - 70% MaxNOM / 30% RVC	- CTH (except from non-originating cathode active materials); or - 50% MaxNOM / 50% RVC	- CTH (except from non-originating active cathode materials) or; - 35% MaxNOM / 65% RVC

Chart 21 **Expected Tariff Liability – SMMT survey (£millions)**



requirements and tariffs would apply to a large number of electrified vehicles traded across the Channel. Electrified passenger cars, buses and commercial vehicles could face additional duties ranging between 10%-22%.

Expected tariff liabilities would represent a major strain on EU and UK EV competitiveness in the respective markets. An SMMT survey estimates that additional tariffs for the 2024-2026 period could amount to £4.3 billion, with £3.6 billion duties charged on imports of EU-built EVs shipped to the UK and £700 million on exports from the UK to the EU. Potential total liabilities could increase to £4.6 billion if impacts on trade with Turkey are included, as the UK-Turkey FTA incorporates identical origin requirements. The EU automotive industry has assessed potential liabilities on exports from the EU at € 4.3 billion.

According to SMMT's own estimates, if all BEV cars exchanged across the Channel were subject to tariffs from January 2024, additional duties would increase the average price of EU-made BEVs on the UK market by more than £3,400, while UK-built BEVs would face an average price uplift of almost £3,600.

While the tariff bill would be particularly hefty for producers and consumers, the cost of backtracking from tariff-free trade of EVs on the credibility of the respective environmental agendas could be much higher, as bilateral tariff-free trade in ICE vehicles would be effectively incentivised to the detriment of trade in less polluting vehicles.

On the UK side, with the introduction of progressively more demanding zero emission vehicle (ZEV) sale targets also scheduled in January 2024, the combined impact of additional tariffs and the new ZEV mandate risks causing a supply-side shock. There is a risk that EU manufacturers would reduce the offer on the UK market of both ZEV and non-ZEVs cars to avoid penalties, reduce tariff impacts and remain profitable, while non-EU suppliers of BEVs might see their market shares increase dramatically.

Finally, while the progressive introduction of more demanding origin requirements can encourage additional investment in e-mobility supply chains, the imposition of tariffs would trigger immediate cost-mitigation strategies, potentially pushing OEMs to source more price-competitive batteries from Asia, rather than incentivising battery and chemical manufacturers to invest in Europe.

RECOMMENDATION 01

TCA ORIGIN REQUIREMENTS FOR BATTERIES

The UK and the EU should agree urgently upon to delay the introduction of tougher battery rules of origin for three years.

SLASHING EV TARIFFS BEYOND THE EU

While addressing the most immediate issues in EV trade with the EU is the sector's top trade priority, ensuring that other FTAs are fit for trade in EVs is crucial to reduce costs for manufacturers and consumers through further tariff slashing and by building economies of scale.

In this regard, modernising existing continuity agreements and negotiating FTAs from scratch with new trading partners can represent a significant opportunity.

First and foremost, when negotiating new agreements, progressive tariff reduction in trade of EVs and batteries should be an essential demand in market access discussions. The value of new FTAs would be significantly diminished should the parties exclude EVs from future liberalisation.

However, even when full liberalisation is agreed, significant commercial opportunities can be achieved only by agreeing origin requirements reflective of the UK's supply chain.

UK-built EVs can avoid tariffs in trade with preferential trading partners either by setting facilitative origin requirements for finished vehicles or by agreeing exceptionally liberal rules for battery packs – or a combination of both. Provided that final rules are broadly achievable, the use of phase-in periods or other flexibilities can also support market opening while encouraging investment to increase domestic value-added.

With the exception of the TCA, where 2027 rules for BEVs and Plug-in Hybrids (PHEVs) are even more demanding than those applicable to ICE vehicles, end rules applicable to EVs under UK FTAs are aligned with rules applicable to traditional vehicles, with the content requirement for most agreements ranging from 50%-60% regional value-added. Even when EU content can be accounted for to meet these origin requirements, this facilitation is not enough to ensure EVs can qualify, either because rules on EVs are simply too demanding, or because European-assembled battery packs are unlikely to meet the FTAs origin rules for batteries, including in trade with Euro-Mediterranean trading partners.

The only exception are origin requirements for finished vehicles agreed in new FTAs with Australia and New Zealand. Under these deals, a 25% regional value-added is enough for an EV to get preferential treatment. Despite the lack of a clause allowing EU cumulation, the rule has been welcomed by UK manufacturers and broadly considered achievable even when progressively more stringent rules for batteries are introduced under both deals over seven years.

Regardless of adjustments to existing FTAs and the achievement of more appropriate origin requirements in new agreements, increasing UK value-added and originating components is the only way to ensure businesses can benefit from both the TCA and trade agreements with the other preferential trading partners in the future. Investment throughout the battery supply chain is essential to ensure UK-made EVs can meet origin requirements and avoid tariffs, with the urgent need for a UK advanced manufacturing strategy aimed at attracting local production of cells, anodes, cathodes, active cathode materials, separators, electrolytes and future battery technologies.

Table 3 **End rules applicable to EVs - selected UK FTAs**

25% Regional Value Content (RVC)	**45% maximum non originating content (MaxNOM) 55% RVC with the possibility to cumulate EU content.**	**40% MaxNOM - 60% RVC with EU cumulation**	**50% MaxNOM - 50% RVC with EU cumulation**
- Australia - New Zealand	- Canada - South Korea - Switzerland - Japan - Singapore - Vietnam	- SACUM bloc, including South Africa - PEM countries excluding Switzerland and Turkey - Mexico - CARIFORUM - ESA - Chile	- Andean countries (Colombia, Peru, Ecuador) - Central America

RECOMMENDATION 02

ACHIEVE FTAs FIT FOR EVs

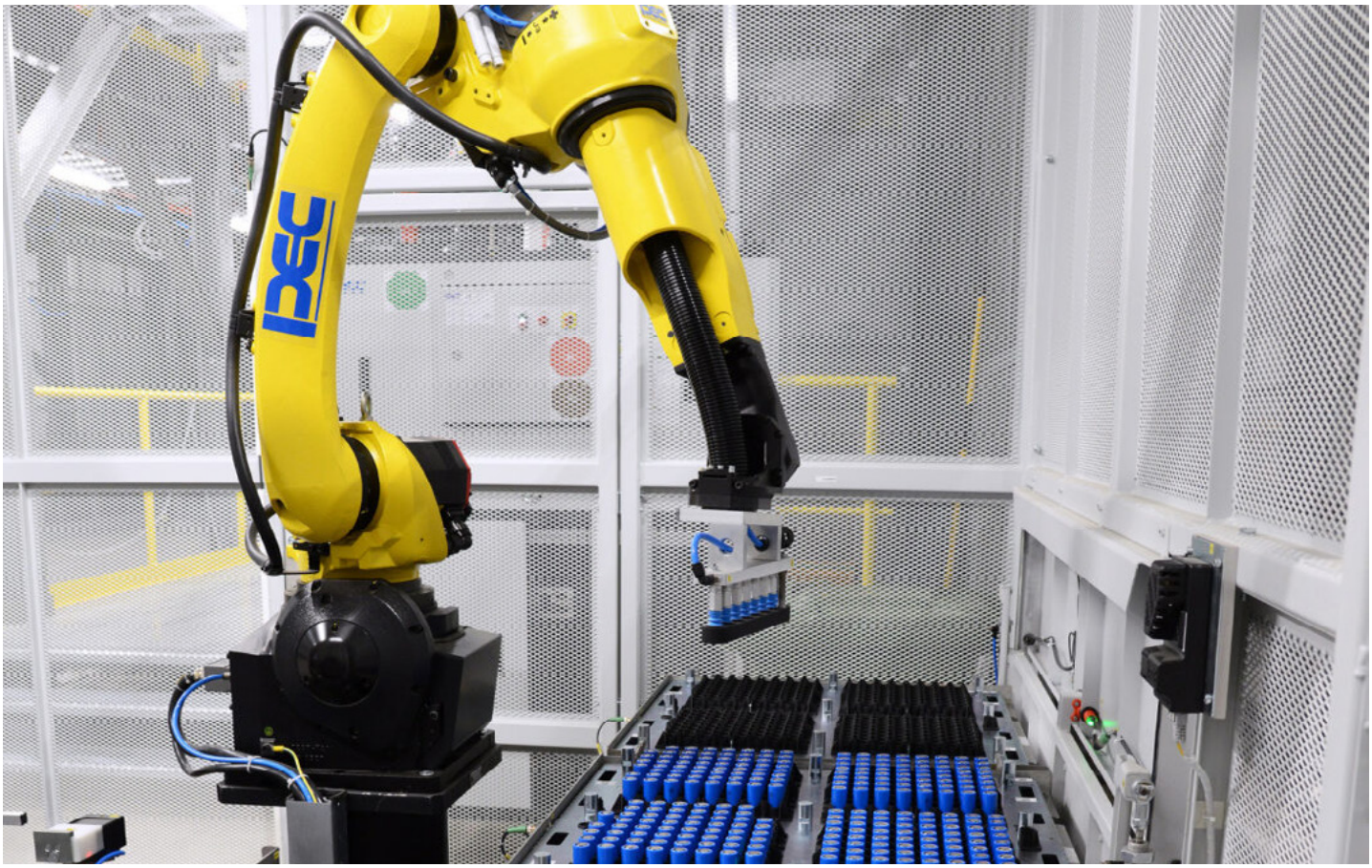
Ensure new and revised FTAs deliver enhanced market access and workable origin requirements for EVs, batteries and related components.

RECOMMENDATION 03

INCREASE UK VALUE-ADDED

Devise a national advanced manufacturing plan to attract additional investment throughout the battery supply chain and ensure the automotive sector can fully benefit from all UK FTAs.

A NEW TRADE POLICY FOR NEW SUPPLY CHAINS



→ **Automotive supply chains and distribution channels remain vulnerable to external shocks. The move to electrification could create additional chokepoints due to the reduction of parts and the concentration of critical raw and refined materials in a handful of countries.**

→ **Strengthening the UK and broader European value chain is crucial to reduce dependency on a limited number of suppliers. However, as imports will remain indispensable, the creation of a critical minerals international network could help weather future storms.**

→ **Recycling and remanufacturing are the cornerstones of a sustainable and resilient automotive business model. However, traditional trade policy instruments are unfit to build an international circular economy and tailor-made solutions are dearly needed.**

RESILIENCE vs ROBUSTNESS

The effects of the global pandemic and its fallout of semiconductor shortages; the war in Ukraine, and its impacts on the international price of essential commodities and the sudden lack of parts such as wire harnessing and neon gas; the most recent restrictive measures between the US and China on chip technologies and materials such as gallium and germanium – all of these external shocks laid bare the vulnerability of the automotive industry's just-in-time, just-in-sequence model.

Global automakers have proved to have a significant level of resilience, with OEMs and suppliers able to readjust their business model and recover lost ground following a major external shock. However, the last three years have shown that the sector is not sufficiently robust to mitigate against a major downturn and avoid grinding to a complete halt if production and sales channels are severely impacted.

Following the pandemic, policymakers have turned their attention to vulnerabilities resulting from the concentration of key inputs of production in a single location, as these chokepoints can represent a significant weakness. In addition to challenges from global health crisis or natural disasters, heightened geopolitical tensions make the weaponisation of reciprocal dependencies between competing powers all the more likely, with the automotive industry at high risk of paying a significant cost.

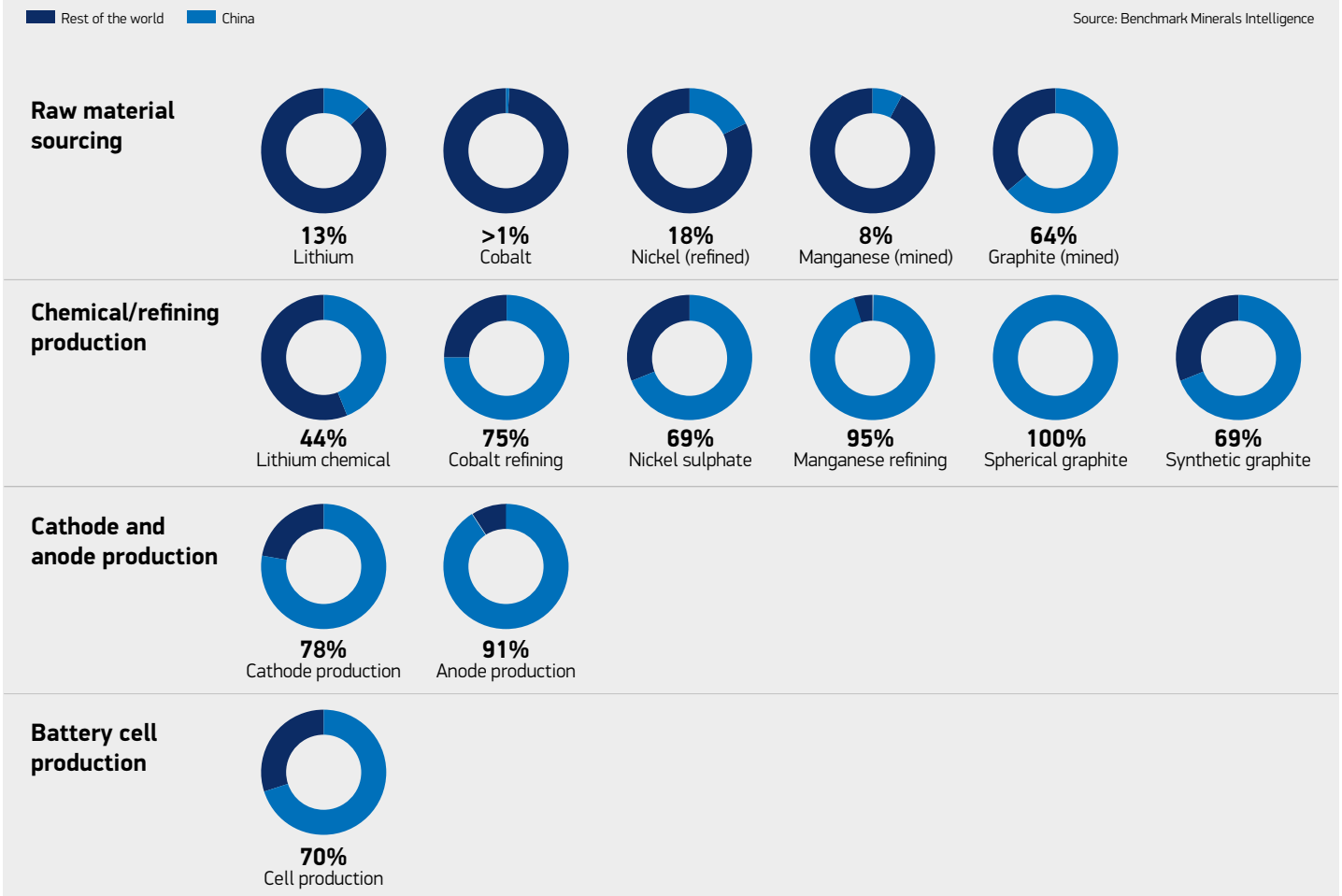
From a supply chain vulnerability point of view, supply chains' electrification is likely to fuel such concerns.

First, the shift from traditional powertrains to e-powertrains will result in a significant reduction in the average number of parts, with potentially fewer alternative suppliers available in case of major crises and less flexibility in the supply chain.

Second, critical minerals needed for the production of batteries and battery parts are extracted from a handful of countries. Lithium is mined largely in Australia and Chile, cobalt in Congo and Australia, and nickel in Indonesia and Russia.

Third, China dominates in minerals refining capacity, with up to 90% of the world's critical minerals refined and processed there.

Chart 22 **Lithium-Ion battery value chain, China vs Rest of the World % of supply**



ADDRESSING THE GREAT MATERIALS DISCONNECT

There is no silver bullet to address potential vulnerabilities throughout the battery supply chain.

Increasing local and regional output could be part of the solution. Stepping up investment is also important to making full use of existing and future FTAs, as more domestic value-added would help to meet origin requirements and avoid tariffs on exports.

Britain already has a foundational EV supply chain, one which is mapped for the first time in SMMT's EV Supply Chain Directory. This shows the UK has the capability to produce almost every component required to manufacture zero emission vehicles in some capacity: batteries, power electronics, hydrogen fuel cells, everything from anodes to graphene to silicon carbide wafers, are already made here in varying quantities and states of industrialisation.

The announcement of a new gigafactory to be built by Tata Group in Somerset has been hailed as a shot in the arm for the UK automotive industry. Together with AESC investment in Sunderland, there is potential to anchor EV manufacturing in the UK and scale up the British EV supply chain. Investment in the whole European region is increasing, with more than 30 gigafactories either planned, in construction or already operating.

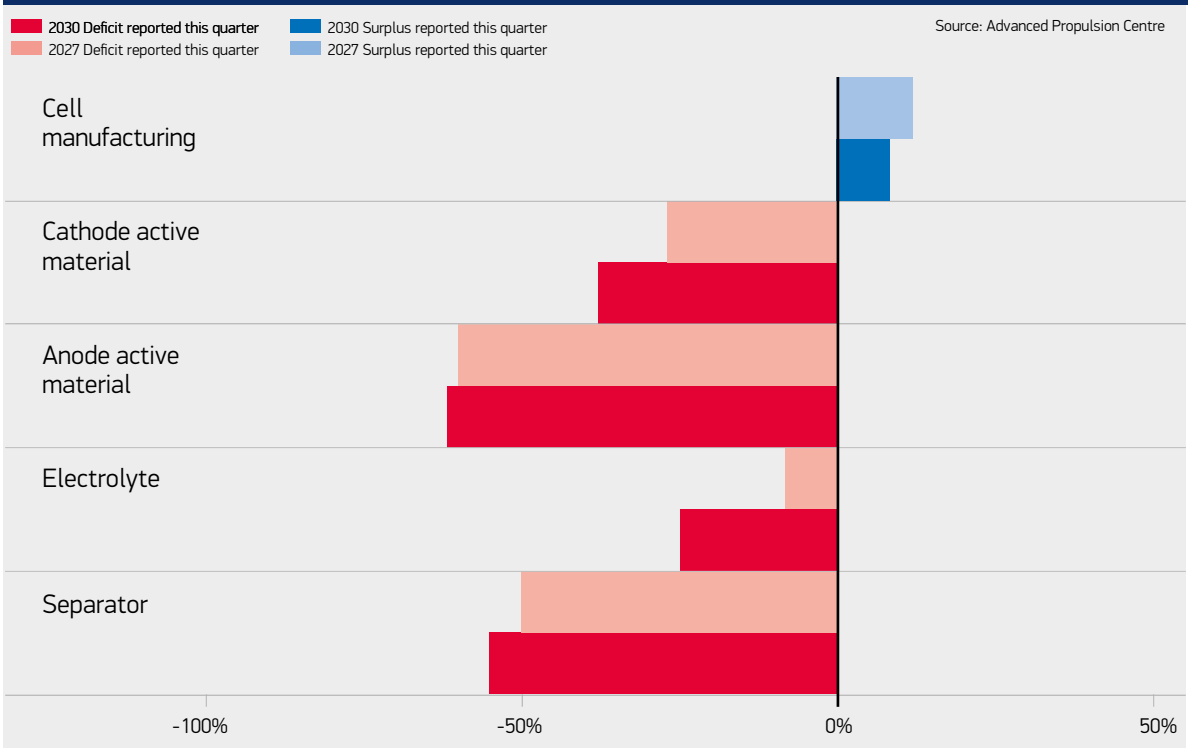
A report by the Advanced Propulsion Centre at the beginning of 2023 shows that the tide might be turning on cell manufacturing, with regional production capability potentially exceeding demand in 2027 and 2030. However, despite significant investment, major gaps remain in expected regional production of critical parts such as Anode Active Materials and separators, as well as Cathode Active Materials.

Further upstream, extraction of critical raw materials will continue to take place in a limited number of countries for the foreseeable future.

The UK does have limited domestic quantities of lithium and graphite, which should be at the centre stage of domestic mineral exploration, mining and refinement projects. However, like many automotive hotbeds, Britain's domestic resources alone will not be sufficient to deliver on the industry's ambition or potential.

In sum, imports are indispensable today and will remain important in the future. Provided that UK and regional capacity will significantly increase over time, the fact that self-reliance is not achievable is not necessarily negative. Radical de-risking strategies aimed at localising the entirety of refining and middle-stream operations in specific countries would likely be extremely costly and potentially ineffective to strengthen the supply chain. Concentration in the UK and Europe would diminish risks of commodity weaponisation but ultimately create another chokepoint that would be subject to all other vulnerabilities.

Chart 23 **2027 and 2030 European capacity vs demand balances**



BUILDING AN INTERNATIONAL CRITICAL MINERALS NETWORK

National critical minerals frameworks such as the EU Critical Raw Materials Act or the UK Critical Minerals Strategy also recognise the need to increase collaboration with other countries, while seeking to enhance domestic capabilities and reduce overreliance on a single trading partner. A more varied portfolio of suppliers of raw and refined critical minerals would enhance both resilience and robustness of the supply chain. At the time of writing, the UK is expected to publish a Supply Chain and Import Strategy by the end of 2023 and is developing a dedicated Battery Strategy.

While the diversification of critical minerals sources depends largely on the mining sector's ability to mobilise significant capitals to explore new deposits and invest in major extraction projects, trade diplomacy can play a role.

Soft instruments such as investment partnerships and memoranda of understanding can facilitate B2B engagement and the mobilisation of capitals for the exploration of prospect extraction hubs and the development of extraction capabilities. It could also lead to collaboration to modernise processing technologies and further integrate battery supply chains. While many similar initiatives have been announced, unfortunately the terms of the partnerships often remain undisclosed. For example, the UK-Canada critical minerals partnership signed in March 2023 has significant potential, but its terms remain confidential. A notable exception is the 2022 Memorandum of Understanding signed between the EU and Kazakhstan, an instrument that can serve as a good template for similar initiatives.

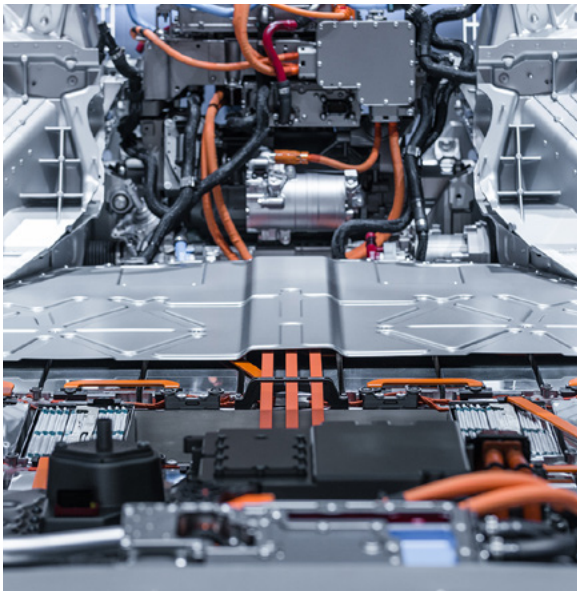
Other bilateral agreements seek to establish more firm commitments to collaborate on trade, investment, environmental and labour policies impacting the development of a critical minerals industry. The US-Japan Agreement on Strengthening Critical Minerals Supply Chains includes an obligation not to impose export duties on five critical minerals, a requirement to discuss measures to address non-market practices from third countries and an obligation to discuss best practices on the review of foreign investment in critical minerals to assess potential national security impacts. The EU and the UK have both announced the negotiation of critical mineral partnerships with the US.

While a commitment to avoiding export duties provides increased certainty, similar agreements could include additional WTO+ commitments that could enhance supply chain reliability. Beyond export duties, a ban on other forms of export restrictions would protect the supply chain from export quotas, voluntary export restrictions or the unjustified suspension of exports tout court, as these measures can exacerbate challenges from unexpected shortages. National treatment obligations for the respective investors and business operators could also add value to a binding agreement. In particular, the parties could reinforce commitments to: non-discriminatory treatment of the counterpart's investors in the mining/processing sector; non-discriminatory treatment in licensing procedures; and fair pricing practices for raw materials sourced by the other party's businesses, versus domestic processing and downstream industries.

RECOMMENDATION 04

CRITICAL MINERALS NETWORK

Agree new critical minerals partnerships with resource-rich countries and major EV markets, seeking both soft and binding commitments to encourage investment and enhance supply chain reliability.



ENABLING AN INTERNATIONAL CIRCULAR ECONOMY

Recycling of critical minerals and remanufacturing of batteries and key components is an essential element to creating a modern circular economy and increasing supply chain reliability. A healthy circular economy can offer price-competitive remanufactured products and reintroduce large quantities of critical materials as key production inputs for manufacturers. This offers major benefits for the environment and preserves the possibility to operate even when suppliers of new materials face stoppages due to a major crisis.

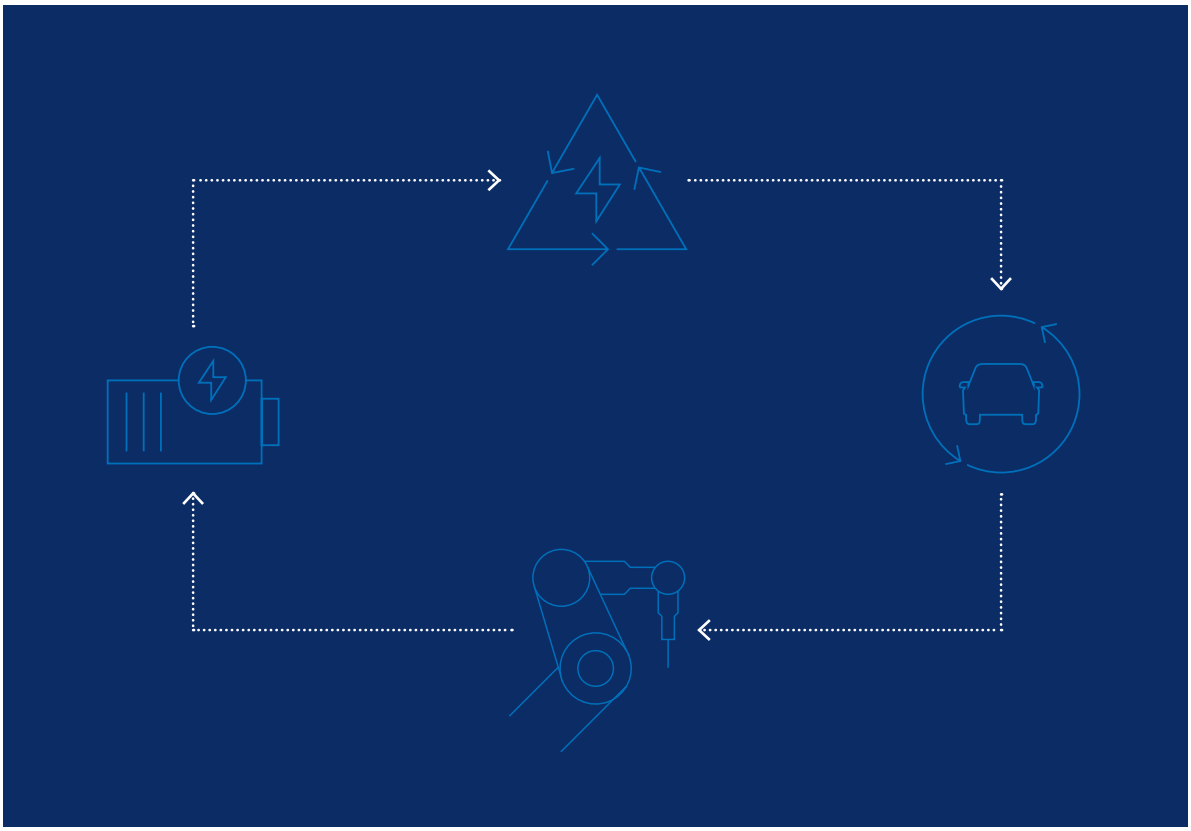
However, limiting recycling and remanufacturing operations to used, worn or otherwise discarded materials available on the UK domestic market drastically reduces the industry's ability to scale up operations. In this regard, the imposition of duties on imports of automotive products that have no commercial value at the time of import results in a major brake on this industry's potential.

Notably, in January 2023, the UK has granted a tariff suspension on imports of used engines, used calipers and worn tyres for remanufacturing purposes, in a major step towards a new trade policy fit for the circular economy. However, tariff suspension application windows are not scheduled regularly and there are no binding commitments on decision timelines, with the final decision taken almost 18 months from the initial application and a second application window opened two years after the first one. End-use suspensions are also complex to apply, with little flexibility on the period of discharge and burdensome authorisation procedures generally unfit to serve the industry.

A more predictable tariff suspension mechanism would greatly support this industry segment. However, a more ambitious plan would be to devise a dedicated strategy to identify potential cost reduction opportunities for all imports of used products that are necessary to scale up remanufacturing and recycling operations.

As part of this strategy, the UK should seek new export opportunities and enhanced market access for remanufactured goods, removing unnecessary import restrictions against used goods in export markets and ensuring that FTAs offer the right conditions to avoid tariffs on exports of remanufactured products.

Global automakers have proved to have a significant level of resilience, with OEMs and suppliers able to readjust their business model and recover lost ground following a major external shock



RECOMMENDATION 05

INTERNATIONAL CIRCULAR ECONOMY

Support the circular economy by streamlining the tariff suspension mechanism and devise a tailor-made strategy to reduce costs of international sourcing of materials needed by remanufacturers and recycling companies.

GLOBAL AUTOMOTIVE TRADE AND THE ROLE OF GLOBAL BRITAIN

→ **The UK automotive sector is well positioned to capture future global growth in Europe, Asia and North America. The UK's accession to CPTPP, the modernisation of agreements with South Korea, Mexico and Canada as well as negotiations with India and the Gulf Cooperation Council could offer enhanced market access and commercially meaningful opportunities.**

→ **With few exceptions, international trade diplomacy is shifting its focus from traditional FTA negotiations to other priorities, including trade-related investment measures, level playing field instruments and new corporate sustainability obligations. Engaging with key trading partners is crucial to enhance cooperation, support the achievement of legitimate objectives and reduce risks of overburdensome barriers to international trade.**

→ **Regulatory challenges and taxation can greatly reduce market access and even offset FTA benefits, with producers of luxury and sports vehicles particularly exposed to non-tariff barriers and behind the border measures.**

THREADING THE NEEDLE: AUTOMOTIVE TRADE IN ASIA AND THE INDO-PACIFIC

Asia is set to be a dominant player in the automotive future, with increasing sales, production and exports to the rest of the world.

Driven by China's automotive expansion, Asia is set to dwarf all other production and sales growth markets. Compared to last year, Asian producers are expected to assemble 3.1 million additional cars in 2025 and 8.9 million additional vehicles by 2030. The region is expected to record very similar increases in terms of new sales over the same period, with 3.1 million more units sold by 2025 and a 8.8 million increase in sales by the end of the decade.

China has held its position as the world's largest automotive market and car manufacturing hub for several years and, after making significant inroads in European markets, China became the largest car exporter too, overcoming Japan for the first time in the first quarter of 2023. The China Association of Automobile Manufacturers reported a 58% increase in exports of motor vehicles compared with the first quarter of 2022, with 1.07 million units destined to markets overseas. The gap has grown further over the first half of the year.

Despite recent headwinds and economic turmoil, China is expected to increase its annual domestic output by more than 3.6 million units between 2023-2028, from 23.8 million cars this year to 27.5 million units (a net rise of over 10 million units over the five years). Sales of new cars in China are expected to increase by more than 3.1 million units over the same period (GlobalData), suggesting an increasing focus on exports.

China's pivoting from a largely inward-focused production centre to the world's largest export hub is likely to prompt increased scrutiny on the sector's business model and China's industrial strategy over the last two decades. The rapid increase in market shares of new Chinese entrants – in particular in the EV segment – bears a tangible risk of increasing tensions in trade between China, Europe and North America, further compounded by China's dominant position in the production of batteries and related parts.

Chart 24 **Global car assembly outlook (Q2 '23)**

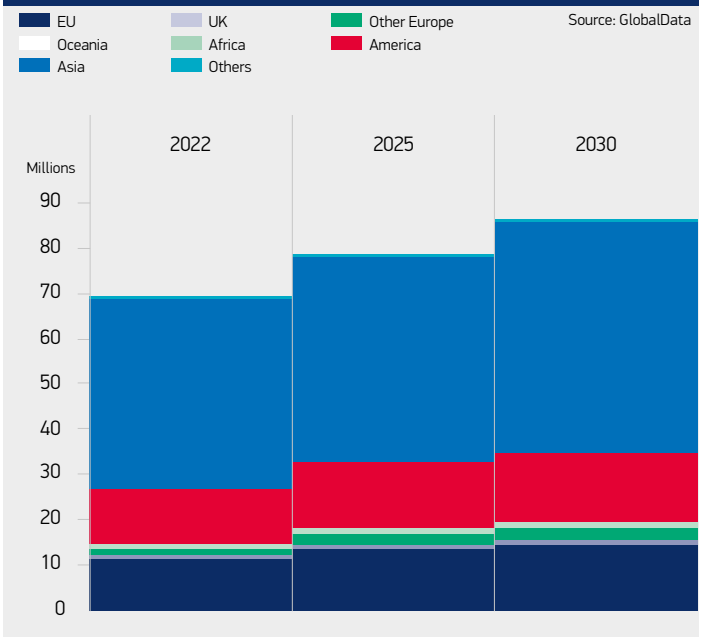


Chart 25 **Global passenger vehicle market outlook (Q2 '23)**

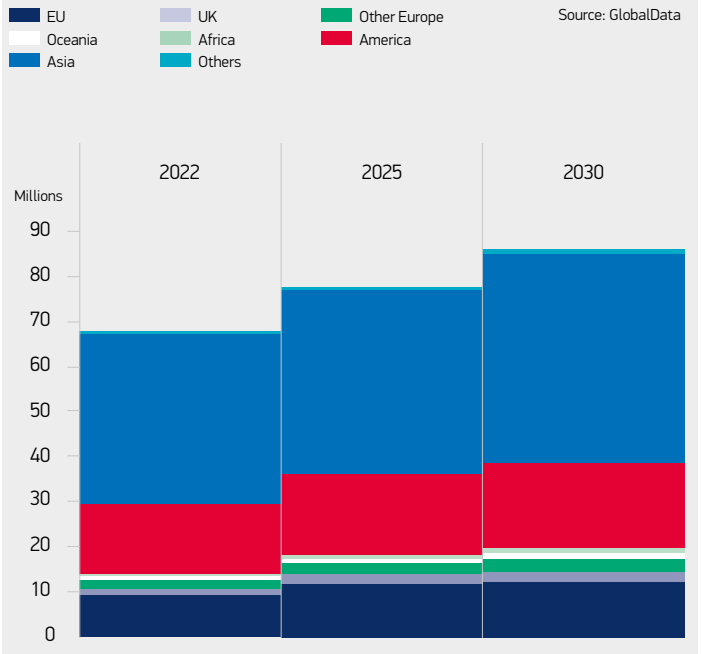
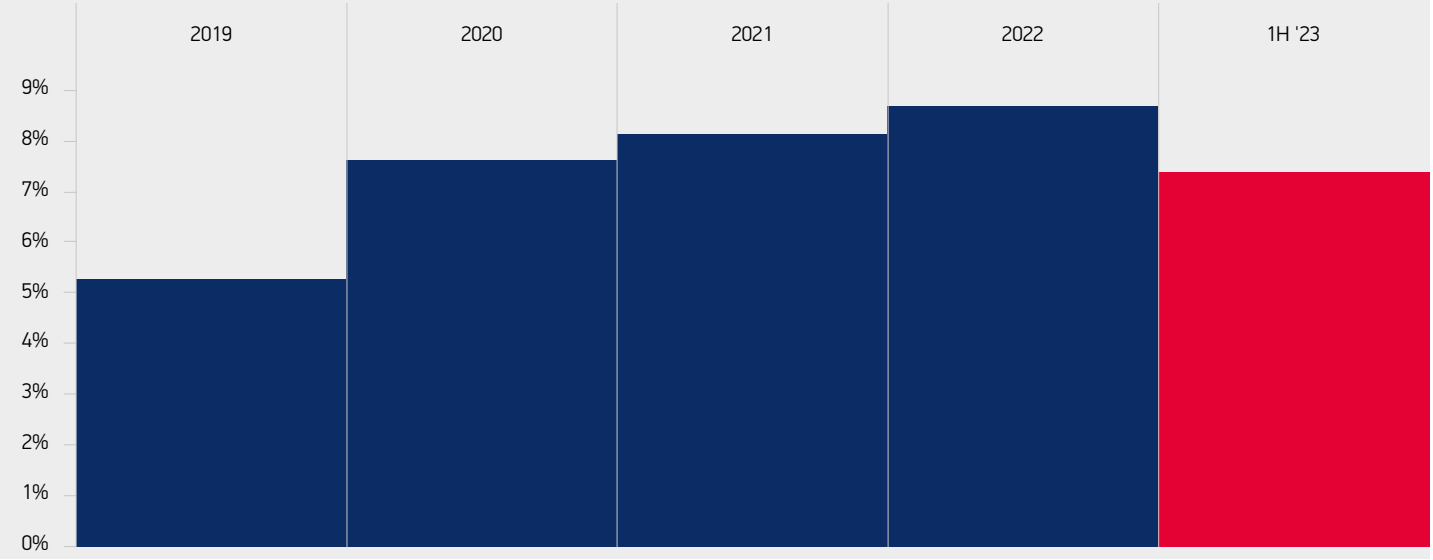


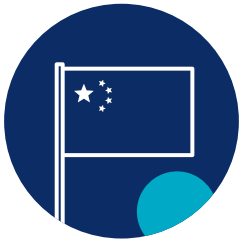
Chart 26 **UK car exports - % to China**

Source: SMMT



The recent announcement of an anti-subsidy investigation on imports of Chinese-made EVs by the President of the European Commission is a clear indication of increasingly tense automotive trade relations. The recent extension of subsidies for purchases of so-called New Energy Vehicles (NEV) to 2027 in the world's most competitive EV market and production hub has fuelled fears that the $72 billion tax break scheme might ultimately result in increased overcapacity of Chinese EV manufacturers, although encouraging domestic demand could also ease pressure on Chinese producers to sell their EV stock overseas.

In this context, the UK remains an open market and the automotive industry has consistently advocated for free and fair trade. However, increasing export opportunities for European-made vehicles could help diffuse tensions. Unfortunately, taking into account that China's domestic market can be served through local investment, there is little evidence that UK-based manufacturers are capturing significant opportunities in this booming market. Although China's share of total UK car exports has risen from 5.3% to 8.7% over the 2019-2022 period, the relative growth was compounded by the major decline in exports to the US, with absolute export volumes actually remaining below pre-pandemic levels in a period of significant expansion following the end of the great lockdown. Furthermore, the share of UK car exports to China has slipped to 7.4% of all outbound shipments in the first half of 2023. While some premium brands are recording positive export performances, the overall trend has fuelled concerns about the attractiveness of UK-made vehicles in China.



RECOMMENDATION 06

ENGAGING WITH CHINA

Monitor potential adverse impacts on the UK automotive industry from the EU's investigation into Chinese EV subsidies. UK manufacturers should support engagement with China by providing meaningful insights into market challenges. Enhanced bilateral dialogue could help address market access barriers.

Despite the undeniable success in becoming a global automotive powerhouse, the Asia Pacific continent has not yet settled its position on regional integration. Beyond China, major players such as India, South Korea and the Asian parties to the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) seek the right balance between automotive business opportunities, trade openness and growing geopolitical tensions.

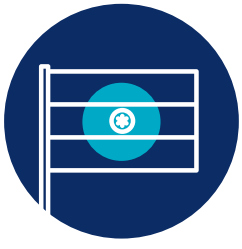
India's automotive sector has many reasons to be optimistic about its future. According to GlobalData, the Indian new car market is expected to rank second in Asia in 2023, just above Japan with 3.9 and 3.8 million units registered respectively. India is expected to consolidate this position by 2028, adding more than 700,000 new vehicle sales, compared with an additional growth of just over 225,000 units in Japan. In terms of production, India is the third biggest Asian manufacturer, following China and Japan but already producing more vehicles than the Korean automotive powerhouse (an expected 4.5 million cars in 2023 compared with 3.6 million). Indian OEMs should turn out almost a million more cars, an increase of a fifth, at 5.5 million units in 2028.

According to the Indian Automotive Component Manufacturers Association, the Indian auto-components industry is worth $56 billion. This market segment grew 23% year-on-year in 2022, with an exceptional export performance worth $19 billion, recording a 42.9% annual growth rate. Indian components are already exported globally. Shipments to North America and the European regions topped the list of Indian components' export destinations, increasing by 46% and 39% respectively – a sign that Indian suppliers are already able to service and be competitive in these markets.

While India decided not to join major regional agreements such as CPTPP and RCEP, Delhi's government has stepped up engagement in trade negotiations after several years of isolationism. The conclusion of FTAs with the UAE and Australia are clear indicators of a renewed interest in enhanced economic cooperation. However, the automotive sector has broadly remained closed, with specific carve-outs allowing India not to liberalise its domestic automotive market.

The outcome of ongoing FTA negotiations will ultimately shape the Indian automotive sector's approach to international markets for years to come. With the Indian domestic automotive industry increasingly bullish on its future market forecast, the successful conclusion of an FTA with the UK could offer mutually beneficial, commercially meaningful opportunities by agreeing progressive tariff reductions on a reciprocal basis and by setting workable origin requirements.

With Indian and into British investors having injected major resources into the development of the respective automotive sectors and the prospect of further supply chain integration – including in EV and battery technology – the UK and India can open the road and build a fruitful bilateral automotive trade relationship. A balanced deal could serve as the basis to remedy a disappointing trade performance for finished vehicles, with India not exporting cars to the UK since Ford's decision to halt shipments in 2020, while the UK has consistently exported fewer than 1,000 vehicles to a market of more than 1.4 billion people due to insurmountable tariff barriers.



RECOMMENDATION 07

OPEN ROADS TO INDIA

Step-up engagement to reach a balanced, commercially meaningful agreement with India providing additional market access across all automotive products on the basis of workable origin requirements.

With regard to CPTPP, the accession of the UK as the first party outside of the Asia-Pacific region, shows the deal's lasting potential to become a catalyst for different economies. With China, Taiwan, Ecuador, Costa Rica, Uruguay and Ukraine having already submitted an application to join the trading pact, and South Korea, Thailand and the Philippines expressing interest in potential accession talks, CPTPP seems the only regional trade agreement with the potential to set future minimum global standards in areas either not covered by the WTO agreements or in great need of modernisation.

Regardless of the geopolitical implications of future accession processes and the UK's approach to these discussions, the negotiation of the UK's accession protocol followed a thorough procedure, with the original CPTPP parties setting a high bar for all future accession processes. The core CPTPP obligations remain unchanged, and any existing or future candidate is unlikely to be able to negotiate its way out of the most impactful commitments. However, CPTPP also showed the necessary level of flexibility to allow expansion without compromising its overall framework.

Specifically, the UK automotive sector's key interests were achieved with minor tweaks to the deal. The alignment of tariff phase-out periods for imports of Japanese cars and light commercial vehicles with the UK-Japan continuity agreement has preserved the balance achieved in the bilateral deal. In addition, the negotiation of a side letter with Malaysia has set a more liberal origin rule for passenger cars, allowing preferential tariffs to apply if the vehicles can meet a 25% regional value content threshold, in line with new FTAs with Australia and New Zealand.

Although the UK's signature was welcomed by the UK automotive industry, potential benefits should not be overstated. As of June 2023, cumulative exports of UK-built cars to CPTPP amounted to 9.6% of all our exports. With the ratification process likely to take at least a year from formal signature, potential gains will not be immediate. As the UK currently already has in place bilateral agreements with nine out of 11 CPTPP members, preferential treatment in Malaysia is one of the most significant opportunities. However, tariff phase-out will take place over several years.

The UK's accession could offer opportunities to businesses with supply chains spanning to the Asia-Pacific region, thanks to the possibility to use content processed in any CPTPP member to meet the origin requirements of the deal. However, CPTPP rules of origin do not allow cumulation of EU content and, for those businesses without significant production inputs from the CPTPP region, meeting CPTPP origin requirements will be challenging without significant investment in the UK to increase domestic content.

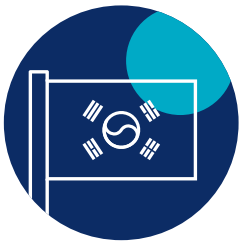
Beyond CPTPP parties, South Korea remains a major automotive hub, with Korean brands expanding manufacturing operations well beyond their domestic market and recording major advancements in India, the US and in Europe. Korean-based manufacturers are expected to increase domestic production by some 200,000 vehicles in the next five years, and new sales should grow by more than 150,000 units over the same period.

South Korea remains one of the most significant export markets with a Free Trade Agreement in place with the UK. Despite a significant downturn in 2020, exports of UK-built vehicles can regain momentum following an adjustment to post-Covid sales strategies.

The announcement on 16 October 2023 of an agreement between the UK and South Korea to extend the possibility to cumulate EU content to meet origin requirements for two more years preserves the continued application of the FTA. Without such extension, British and South Korean-based manufacturers were at risk of facing tariff liabilities worth tens of millions of pounds from January 2024.

However, as renegotiations to modernise the UK-South Korea deal are yet to start at the time of writing, it is imperative for the parties to launch, finalise and ratify a new agreement before the expiry of the extension to avoid the reintroduction of tariffs. Looking ahead, regardless of whether EU cumulation clauses will be retained at the end of the renegotiations, the UK and South Korea should agree on origin requirements that allow electrified vehicles and batteries to benefit fully from the modernised agreement.

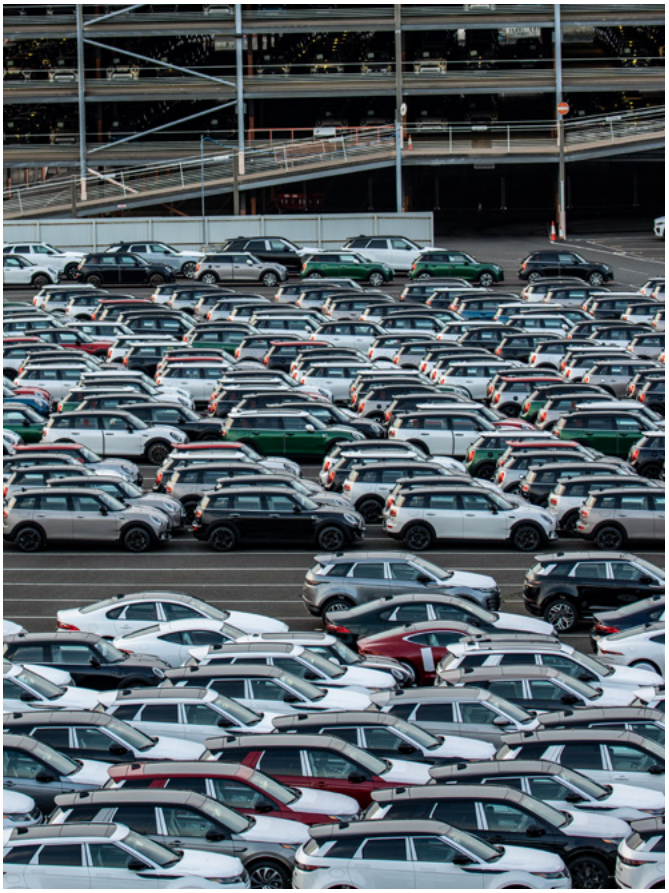
The UK automotive sector is well positioned to capture future global growth in Europe, Asia and North America



RECOMMENDATION 08

TRADE CONTINUITY WITH SOUTH KOREA

Launch, negotiate, finalise and bring into effect a modernised UK-South Korea Free Trade Agreement before the expiry of the extended EU cumulation clause.



SHIFTING THE DIAL: NEW AUTOMOTIVE TRADE PRIORITIES FOR THE OLD WORLD

Despite major headwinds, the EU remains the UK's largest automotive trading partner and a very significant growth market both in terms of production and future sales. According to GlobalData, the EU will capture most of the world's growth in sales of new passenger vehicles in the near future, with a 28.7% increase in registrations in 2025 compared with 2022. In 2030, the EU is expected to be the second largest growth market after China, capturing more than 30% of global growth in new sales compared with 2022 levels.

While EU sales and production figures remain far below pre-Covid-19 levels, GlobalData's car assembly outlook suggests that overly-pessimistic takes on the future of the EU automotive manufacturing sector might be misplaced.

Compared with last year, EU production lines are expected to turn out 2.37 million more passenger vehicles by 2025 – the world's highest increase in volumes over this period. By 2030, the EU could produce an additional 3 million units compared with 2022 and remain the second largest growth market after China.

While the EU continues to seek opportunities to enhance market access in negotiations of new FTAs with countries such as Australia, Indonesia, India and the modernisation of some existing agreements with a number of trading partners, policy makers in Brussels are increasingly focused on a more assertive trade policy with the primary focus on achieving ambitious environmental objectives.

In this context, the European automotive industry is walking a narrow path to maintain an open trade agenda while building a regional electromobility supply chain. In addition to the aforementioned challenges in meeting rules of origin requirements for batteries and EVs, several regulatory initiatives will impact the sector's ability to trade with the rest of the world.

The implementation of the world's first Carbon Border Adjustment Mechanism (CBAM) in October 2023 represents a milestone in addressing carbon leakage and creating a level playing field that adequately takes into account embedded carbon emissions in the production of goods. However, the introduction of reporting requirements in the first phase of the implementation and the obligation to purchase and surrender the appropriate amount of CBAM certificates from January 2026 is likely to add costs and increase automotive businesses' administrative burdens when sourcing key inputs or production such as steel, aluminium, electricity and hydrogen. Moreover, the potential CBAM expansion to more complex products further downstream might have direct impacts on automotive manufacturers in the future.

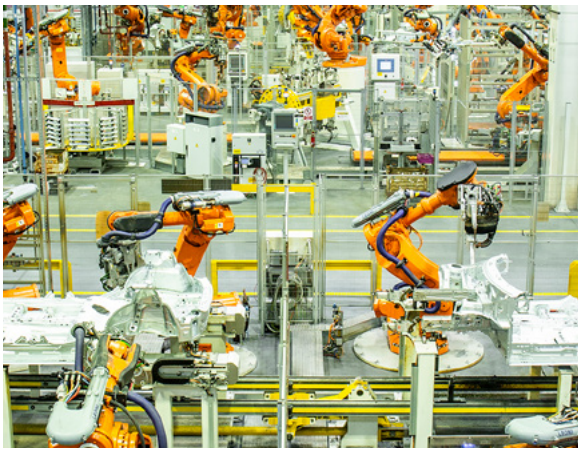
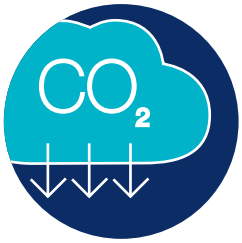


Table 4: **Global passenger vehicle market outlook - by country - volume change (LMC, Q2, 2023)**

Volume change 2022 v		
	2025	2030
EU	2,655	2,800
USA	2,105	2,038
Japan	830	565
China	617	4,748
UK	572	712
India	435	1,255
Russia	307	919
Iran	293	441
Brazil	287	865
Other Middle East	277	519

Table 5: **Top 10 growth markets (car assembly) – LMC Q2 '23**

Volume change 2022 v		
	2025	2030
China	1,352	5,130
EU	2,377	3,035
India	515	1,561
USA	1,180	1,150
Brazil	221	837
Mexico	636	641
Russia	282	610
Indonesia	166	439
Japan	307	429
Thailand	271	395



RECOMMENDATION 09

COOPERATE TO ADDRESS CARBON LEAKAGE

With the UK and several other countries already implementing Emission Trading Schemes and considering the implementation of CBAMs similar to the EU's, European automotive businesses might greatly benefit from the recognition of equivalent regulatory regimes and the reduction of administrative burdens and additional costs in movements of covered products between them.

CBAM will not be the only measure impacting domestic and external operators servicing the EU market, with due diligence obligations being the centrepiece of a number of regulatory developments.

The proposed EU Corporate Sustainability Due Diligence Directive (CS3D) aims to anchor human rights and environmental considerations in companies' operations and corporate governance. The directive is likely to impose obligations on businesses to identify, end, prevent, mitigate and account for negative human rights and environmental impacts of their actions, including in their value chains inside and outside the EU.

While the CS3D is still under discussion, due diligence obligations linked to the new EU Battery Regulation will be fully implemented from July 2025. The regulation requires due diligence of supply chains to assess social and environmental risks, with a key focus on the supply of cobalt, natural graphite, lithium and nickel, as well as chemical compounds derived from them. The responsibility lies with the economic operator that places batteries on the EU market, with a requirement to incorporate the due diligence policy into contracts and agreements with suppliers. In addition, specific labelling requirements will apply to all batteries, while EV batteries of more than 2 kWh will need a digital battery passport storing relevant battery data along the product's entire lifecycle.

Finally, the new EU Deforestation Regulation sets obligations to conduct extensive due diligence on the value chain to ensure certain goods do not result from recent deforestation or breaches of local environmental laws. With products such as rubber and wood covered by the regulation, OEMs and suppliers must put in place the necessary mechanisms to comply with the new obligations and produce a due diligence statement when importing or exporting covered products from December 2024.

While the EU's trade agenda is increasingly focused on establishing a level playing field, neighbouring trading partners in Africa and in the Middle East strive to become new production hubs.

As a whole, the African region remains relatively marginal in terms of global sales. When considering both passenger cars and commercial vehicles, the African Association of Automotive Manufacturers estimated that the entire African new car market amounted to 1.2 million vehicles in 2021, covering just 1.3% of global demand. New sales are hampered by a low motorisation rate, lack of infrastructure and a largely unregulated market of second-hand cars.

Despite these challenges, the domestic automotive sector shows encouraging signs of potential future expansion. GlobalData estimates that African-based OEMs will see car assembly volumes increase by 50.5% in 2025 and 69.8% in 2030 compared with 2022 levels. African-made passenger cars should hit the 1 million units threshold next year, a significant milestone. Notably, two of the nine trading partners supplying the UK new car market are African production hubs, namely South Africa and Morocco.

A renewed emphasis on regional integration could boost opportunities to build a stronger African market and integrated supply chains. The entry into force of the African Continental Free Trade Area (AfCFTA) in 2021 and the development of tailor-made national automotive strategies in countries such as Ghana, Egypt, Kenya and Nigeria could mark a pivotal moment. However, the lack of a dedicated automotive origin protocol has hampered the ability of African-based manufacturers to make use of the AfCFTA pan-continental cumulation provision.

RECOMMENDATION 10

DEVELOP A SUSTAINABLE SUPPLY CHAIN

EU regulations on corporate sustainability are likely to set a new global benchmark. It is essential for automotive businesses operating in the UK and in the broader European region to familiarise with new and upcoming obligations and put in place the necessary compliance mechanisms.

In addition, the technology gap between Africa and leading manufacturing regions is likely to widen as the industry transitions to low emission vehicles. But while the African EV market is unlikely to expand anytime soon, the region can play an indispensable role in EV international supply chains thanks to the high concentration of critical minerals in the continent. Collaboration with automotive hotbeds in the form of partnerships and memoranda of understanding could represent an opportunity to attract funding for the local mining, extraction and refining sector. In addition, resource diplomacy should achieve not just financial capitals and security of supply, but support ethical, clean and sustainable sourcing too.

While Africa is striving to attract investment and build a more mature ICE vehicle market, Middle Eastern players such as the UAE and Saudi Arabia are seeking to leapfrog directly to the electrification phase.

Traditionally dependent on oil production and exports, Saudi Arabia is investing billions to pivot its economy towards an accelerated electrification of the automotive sector, with a plan to install 50,000 EV charging stations by 2025 and an aspiration to become a major regional player in the production of EVs in the medium term. Outward investment into brands such as Lucid Motors and new foreign direct investment in EV battery production testify to the dynamism of the country in its electrification strategy.

Ongoing negotiations between the UK and the Gulf Cooperation Council (GCC) for a new FTA represent a major opportunity to strengthen trade and investment ties with the region. However, infant industry arguments and the lack of short-term offensive interests beyond energy products could reduce the GCC's willingness to reach an ambitious agreement on market access for automotive goods.

RECOMMENDATION 11

TRADE WITH THE GULF

Finalising an ambitious new FTA with GCC countries could open commercially meaningful opportunities if the parties agree on enhanced market access commitments.

CARROT AND STICK: AUTOMOTIVE TRADE PRIORITIES IN NORTH AMERICA

Similar to the EU, the US new car market remains below pre-Covid-19 levels, but it is expected to rank consistently as the world's second largest until the end of the decade.

On the production side, the US is expected to be the fourth largest growth market by 2030, beyond China, the EU and India, capturing 16.4% of global car production growth compared with 2022 levels.

Against this background, successive US Administrations have deprioritised new FTA negotiations, seeking limited sectoral partnerships with more distant trading partners and a more recent focus on EV incentivisation and battery localisation at the regional level.

While maintaining most trade-restrictive measures in trade with China, including additional tariffs on imports of EVs, the Biden Administration has engaged with its closest allies to resolve some of the outstanding bilateral challenges, including agreeing on a pragmatic approach to remove tariffs on imports of EU and UK steel and related European rebalancing measures on typical US products such as motorcycles, whiskey and blue jeans.

The US has neither resumed discussions to accede to the once US-led Trans-Pacific Partnership nor relaunched negotiations with the EU and the UK. Instead, the Administration has launched new initiatives, such as the EU-US Trade and Technology Council and the Indo-Pacific Economic Framework for Prosperity. These fora allow greater coordination on global trade challenges and supply chains, but do not involve discussions on additional market access and trade liberalisation.

However, the adoption of the US Inflation Reduction Act (US IRA) in 2022 has caused significant concerns, with the introduction of a credit mechanism awarding up to $7,500 on sales of clean vehicles assembled in North America if the battery parts and related critical minerals meet strict localisation requirements. Despite an increase in announced inward investment, it is unclear how the US IRA can help the US Administration to meet its stated objective of 50% all-electric vehicles sales by 2030 and the even more ambitious expectations of the Environmental Protection Agency, as credits can be accessed today only on purchases of a limited number of clean vehicles and even more demanding requirements will be progressively phased in.

Although the scheme remains problematic for importers, its impacts on the ability of global EV manufacturers to compete in the US market have been mitigated by the imposition of less burdensome requirements on leased vehicles. In addition, critical minerals producers will be allowed to compete on the same footing with domestic producers if their host countries have a critical minerals partnership in place with the US. Extending this possibility to refined and recycled critical minerals would further mitigate potential negative impacts.

Table 6 **Top 10 new passenger vehicle markets (LMC, Q2 2023)**			
		2022	2030
1	China	23,965	28,713
2	USA	10,738	12,776
3	EU	9,253	12,054
4	India	3,699	4,955
5	Japan	3,445	4,010
6	UK	1,614	2,326
7	Brazil	1,573	2,439
8	South Korea	1,424	1,651
9	Canada	1,161	1,420
10	Iran	996	1,437

Source: GlobalData

Table 7 **Top 10 new car producers (LMC, Q2 2023)**			
		2022	2030
1	China	23,476	28,605
2	EU27	11,356	14,398
3	USA	7,032	8,183
4	Japan	6,583	7,012
5	India	4,348	5,909
6	S Korea	3,399	3,673
7	Mexico	2,220	2,861
8	Brazil	1,811	2,647
9	Indonesia	1,173	1,611
10	Canada	1,129	1,313

Source: GlobalData

RECOMMENDATION 12

BUILD ON THE ATLANTIC DECLARATION

Finalise negotiations of a US-UK critical mineral partnership to improve market access in the US for critical minerals extracted, refined or recycled in the UK.

Looking at the broader North American region, Mexico and Canada are expected to rank consistently among world's top 10 production hubs until the end of the decade, respectively as the seventh and 10th largest manufacturing hotbeds according to Globaldata. Canada will retain its position as the world's ninth largest new car market until 2030, while Mexico is expected to become a 1 million new passenger vehicle market by 2025.

Mexico and Canada have adjusted their own trade agendas to balance the current push for regionalisation with new opportunities across the world. After concluding challenging negotiations to replace the landmark North American Free Trade Agreement during the Trump Administration, Canada and Mexico successfully secured their competitive position in the application of the US IRA by ensuring that localisation requirements for finished vehicles and batteries would extend to the entire North-American region.

Driven by a boom in trade of manufactured goods, Mexico has recently become the US' largest trading partner, capitalising on the fractious US relations with China and nearshoring trends. Thanks to its proximity to the US market, significant critical mineral resources, fully integrated regional supply chains and some 13 FTAs already in place, Mexico has the potential to become an even more prominent automotive production and trade hub. However, similar to its largest trading partner, Mexico has also been lukewarm in seeking enhanced market access abroad, with the UK being a notable exception.

Canada maintains a positive trade agenda, seeking to advance a progressive and inclusive trade policy in addition to improved market access. Despite a major political setback in negotiations with India, Canada continues negotiations with other emerging markets such as Indonesia and Morocco as well as regional trading blocs such as MERCOSUR, CARICOM, ASEAN, Central American states and the Pacific Alliance.

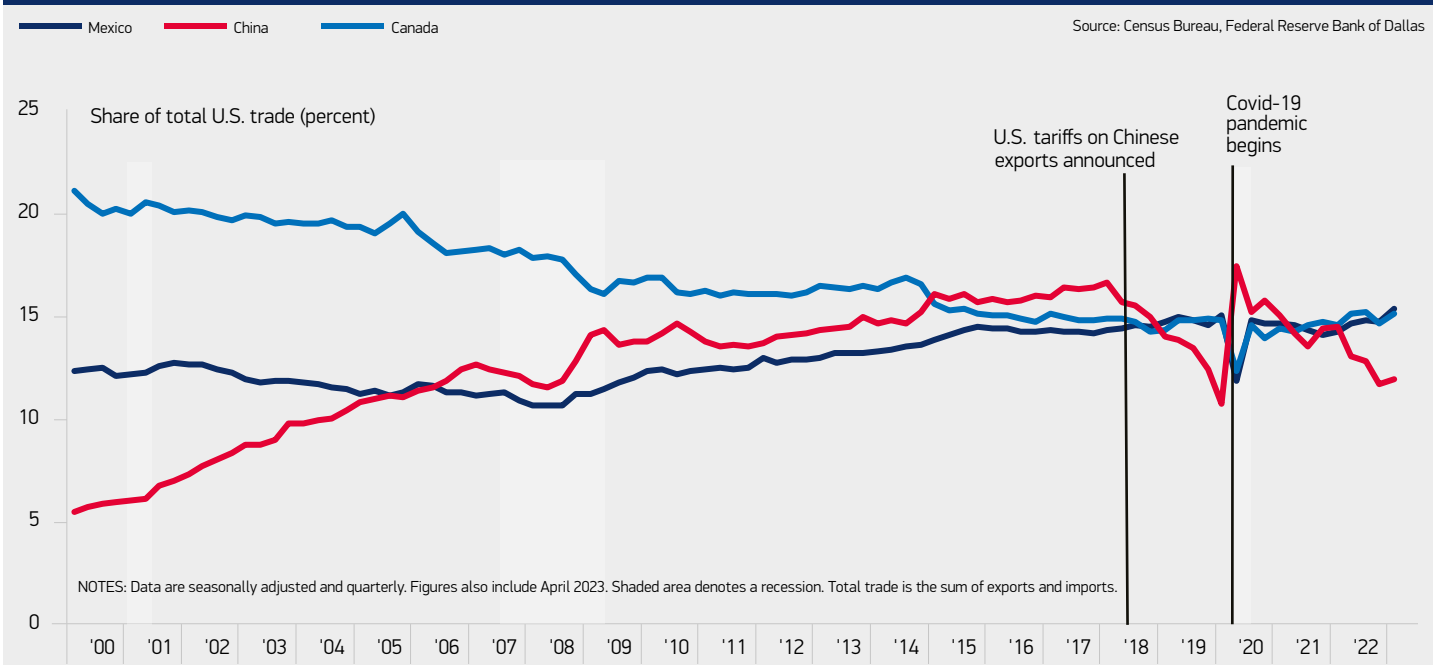
In this context, the UK enjoys a privileged position, with major opportunities to deepen its trading relationship with both countries. Ongoing renegotiations could offer a chance to rewrite the outdated terms of the UK-Mexico FTA, including overdemanding origin requirements for finished vehicles and parts, as well as deliver a dedicated automotive annex to reduce regulatory challenges. Although the continuity agreement with Canada already offers more modern trading terms, an upgraded UK-Canada FTA could achieve enhanced market access for EVs and batteries, deliver additional flexibilities to meet origin requirements and strengthen cooperation on supply chains, including critical minerals. However, while renegotiations are finalised and the new agreements take effect, it is crucial for the parties to ensure continuity of trade by extending existing cumulation clauses allowing businesses to account EU materials to meet origin requirements and avoid tariffs.

RECOMMENDATION 13

REFORGE TRADE TIES IN NORTH AMERICA

Conclude the negotiation of upgraded FTAs with Mexico and Canada and secure an extension of existing EU cumulation clauses to ensure trade continuity until the new agreements take effect.

Chart 27 **Mexico becomes top U.S. trading partner at start of 2023 (Federal Reserve Bank of Dallas)**



REDUCING BARRIERS FOR SMALL VOLUME MANUFACTURERS

The UK hosts some of the world's most renowned small volume manufacturers (SVMs), including quintessentially British brands producing luxury vehicles and sports cars. SVMs tend to have a varied export portfolio, with sales in the EU, America, Africa and Asia – including the Middle East – on the rise in 2022.

With high-profile SVMs producing and exporting from just a handful of countries, only few regulators in key export destinations take into account the specificity of the SVM business model when developing their automotive regulatory frameworks. Accordingly, SVMs are often disproportionally affected by the introduction of burdensome regulatory requirements when export countries do not devise additional flexibilities for SVMs.

Often, the conclusion of an FTA is not enough to address SVM regulatory challenges, with potential tariff gains unable to offset non-tariff barriers or taxation measures affecting SVMs. Examples abound, with regulatory challenges in countries as diverse as Australia, China, Canada, South Korea, Japan, India and Saudi Arabia.

To cite some of the most impactful challenges, the introduction of advanced emergency braking systems (AEBS) or emergency lane keeping systems (ELKS) regulations with tight implementation deadlines and no additional flexibilities could result in major difficulties for SVMs, as a limited product portfolio and long platform development cycles constrain SVMs' ability to make changes without adequate and sufficient notice. The same applies to E-call and Event Data Recorder requirements

A significant challenge is the introduction of luxury car taxes in countries such as Australia and Canada, with disproportionate impacts on imports of premium and luxury vehicles from the UK. In the case of Canada, the issue is further exacerbated by the exaction of a new federal luxury tax on top of pre-existing luxury taxes in some provinces such as British Columbia.

RECOMMENDATION 14

GO TO BAT FOR ICONIC BRITISH BRANDS

Enhance regulatory engagement with key trading partners to seek additional flexibilities for SVMs and mitigate against impacts of overburdensome regulatory and behind-the-border barriers.

Chart 28 **SVM car production by destination**

ANNEX: DATA SOURCES

SMMT has used four key sources for the trade data – ONS, HMRC, APC quarterly estimates and our own SMMT data sets.

SMMT data on car exports to individual EU member states has been amended to reallocate some outbound flows from OEMs who export to regional hubs before further distributing their vehicles

The three government sources are used for value of exports and imports. HMRC and ONS use slightly different classifications and approaches, but the overall difference is relatively small in this context. We have used ONS data for the headline figures and HMRC data for country specific information (which is not available from the ONs data). SMMT data is used for volumes of vehicle production destined for export and new registrations by origin.

For more information on SMMT data and for additional data please contact aisdata@smmt.co.uk.

Regional market forecasts on passenger vehicle sales and production have been kindly provided by GlobalData, **www.globaldata.com**

The ONS data uses the change in ownership balance of payments methodology, while HMRC uses physical movement of goods.

The ONS data uses SIC29 and covers all motor vehicles, including engines and parts and accessories. The ONS data gives both home and export details and a split between EU and non-EU. See https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/bulletins/uktrade/previousReleases for data and http://www.siccodesupport.co.uk/sic-division.php for SIC29 definition.

The HMRC data uses HMRC codes and for the purposes of this report certain codes in 87 (motor vehicles and parts and accessories) and 84 (engines). The detailed codes are given below. See: https://www.uktradeinfo.com/

HMRC Codes used

- 870121 Tractors
- 8702 Motor vehicles for the transport of >= 10 persons
- 8703 Motor cars and other motor vehicles principally designed for the transport of <10 persons, incl. station wagons and racing cars
- 8704 Motor vehicles for the transport of goods, incl. chassis with engine and cab
- 8705 Special purpose motor vehicles
- 8706 Chassis fitted with engines, for tractors, motor vehicles
- 8707 Bodies, incl. cabs, for tractors, motor vehicles
- 8708 Parts and accessories for tractors, motor vehicles
- 8709 Works trucks
- 8716 Trailers and semi-trailers
- 840731, 840732, 840733, 840734 Petrol Engines
- 840820 Diesel Engines

SMMT
DRIVING THE
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