The EU automotive sector in a globalised market

Abstract

Over the past decade, the global car industry has undergone a gradual but significant shift in sales and production numbers from developed into developing markets. This shift has plunged many European car manufacturers into a particularly difficult structural crisis as they have had to grapple with falling domestic sales and growing overcapacity issues. The economic importance of Europe’s car sector underscores the potential damage that this crisis may inflict on many EU member states.

Increasing the volume of exports has been suggested as a solution to the current predicament of Europe’s car industry. This policy briefing provides an in-depth analysis of recent trends and possible future developments in nine mature and growing car markets, concluding that Europe’s car sector could expand its share in a number of these markets.

Tariff and non-tariff barriers, however, pose a significant obstacle to this scenario and their timely removal is of utmost importance for the European car industry. The European Commission included improved market access in its CARS 2020 Action Plan yet the relative ease with which countries can introduce non-tariff barriers remains a cause for concern.
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1. Introduction

The European car sector is experiencing a particularly difficult period. Sales and production numbers have decreased significantly since the onset of the continent’s economic difficulties, imposing a considerable burden on EU carmakers. This burden is two-fold and its effects are closely interlinked, as the collapse in car sales is responsible not only for the carmakers’ financial difficulties but also for the growing overcapacity problem in certain EU15 countries.

Falling sales in Europe contrast with rising sales in developing markets, suggesting that further increasing the volume of car exports could be a solution to the European sector’s current woes. Numerous tariff and non-tariff barriers, however, prevent EU car exporters from increasing their sales in growing and more mature markets and restrict their exports to high-end cars.

This paper will provide an overview of the global and European car industries with a specific focus on recent trends and problems. It will then analyse a number of key European car export market markets and conclude with an overview of trade barriers that hamper market access to these markets.

2. The global car industry

The automotive industry enjoyed a period of steady growth before the onset of the global financial crisis. Production rates increased from 41.22 million units in 2000 to 53.2 million units in 2007, interrupted only by a mild downturn in 2001. The industry was badly affected by the global economic recession and the subsequent decrease in global demand; as production slowed down in the final months of 2008 and fell sharply in 2009 by nearly 5 million units. It should be noted that this decrease was more pronounced that the contraction of the world economy, highlighting the automotive sector’s vulnerability to adverse economic conditions. An important turning point for car manufacturers occurred in 2010, when the fall in production numbers halted. Production rates exceeded their pre-crisis levels by a considerable margin, with 58.34 million cars produced worldwide. The industry grew by 3% in 2011, with 59.95 million units produced. The International Organisation of Motor Vehicle Manufacturers (OICA), the principal industry body, expects this rate of growth to be maintained in the current year.
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Source: OICA data

The recent growth in global demand for passenger cars has been geographically uneven. Sales have yet to recover in the region traditionally seen as responsible for demand — the ‘Triad’ (Japan, the USA and the EU/Western Europe), particularly in the US and the EU. Increasing affluence and demand in developing countries in general, and in China in particular, sustains the sector’s recent recovery and projected future growth. New car registrations in China doubled in two years, reaching 12.55 million units in 2010. Sales in India grew by two thirds, and by one quarter in Brazil, during the same period.

Source: ACEA; Bureau of Transport; National Bureau of Statistics of China; JAMA; Fenabrave; SIAM

The changing geographic distribution of passenger car demand has directly influenced changes in the geographic distribution of car manufacturers’ output. Although the EU has retained its position as the leading global car producer, output in Japan and the US has fallen. South Korea is perhaps the only developed country not to have decreased car production; its production rates have, rather, significantly increased. In this, South Korea resembles a number of emerging economies. Car production in India has increased five-fold, and China, which produced only some 700 000 cars in 2001, has become the global number two producer, with 14.49 million units in 2011. Output in Brazil grew more
The changing geographic distribution of passenger car demand has directly influenced changes in the geographic distribution of car manufacturers’ output.

Although production may have diversified geographically, the global car industry remains dominated by a limited group of suppliers, and these carmakers command a significant presence on most continents in terms of both sales and production. For example, Toyota, Volkswagen and General Motors were responsible for more than one third of global car production in 2010. Volkswagen in particular is projected to strengthen its leading position over the coming years, courtesy of its growing output in Europe,
The EU automotive sector in a globalised market: China, India, Brazil, Mexico and Russia.

As far as the industry’s future is concerned, the issue of overcapacity is casting a long shadow\(^2\). In just ten years, car production in Japan decreased by almost a million of units. US car production fell by two million units within the same time period, and General Motors and Chrysler were forced to file for Chapter 11 restructuring (reorganisation bankruptcy). Many European car manufacturers are also struggling with overcapacity. Although manufacturers such as Volkswagen and Toyota have been able to weather the crisis by increasing their production in emerging markets, these markets are expected to reach saturation at some point in the future\(^3\). China, for example, which was responsible for nearly one quarter of the global car production in 2011, had an estimated six million units of unutilised capacity in the same year — nearly twice the size of the German car market\(^4\). Global overcapacity is forecast to reach 20-30\% by 2016\(^5\) — a rate similar to those already reported by many of Europe’s struggling car manufacturers. Given the car industry’s importance — both in terms of industrial output and employment — to many national economies, many governments may attempt to further protect their industries in the future.

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\(^2\) Overcapacity occurs when the installed productive capacity in a given factory or industry exceeds output, e.g. when domestic sales fall. It can be solved by adjusting the existing installed capacity or increasing the volume of exports to foreign markets.

\(^3\) It should be noted that certain markets might reach their saturation point in terms of high car ownership rates but still manage retain high levels of annual sales, especially under favourable economic conditions (due to high car replacement rates). The US serves as a prime example of this.


\(^5\) KPMG, *Overcapacity – Global Automotive Executive Survey 2012*
In sum, the global car industry has recovered from the world financial crisis, and annual production rates have reached unprecedented numbers. An important geographical shift in sales and output has occurred, from the Triad towards countries such as China and India. Global overcapacity is expected to become a major problem in the near future.

3. The European car industry

Car production in Europe has generally mirrored developments caused by the global economic slowdown, as European output declined by 6.7% to 15.95 million units in 2008 and by 12.8%, to 13.9 million units, the following year. Production rates increased with the global car market's recovery in 2010 and 2011, by 9.9% and 2.7% respectively, but remain over a million units short of their 2007 output. Europe’s automotive industry consists of major indigenous car-making groups, including Volkswagen, Daimler, BMW, Fiat, PSA and Renault, which run car plants in their home countries as well as in new EU Member States (Fiat in Poland, for example, or PSA in Slovakia). Overseas carmakers also operate assembling plants in Europe: General Motors (Opel) in Germany, Nissan in the UK, and Hyundai in the Czech Republic. As the graph below indicates, car production in the EU’s newer Member States has increased significantly over the past five years, but traditional car-producing countries such as Germany and France continue to be responsible for the bulk of European car production.
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New passenger car registrations in the EU have not risen on a year-to-year basis since 2007.

While Europe’s car output has recently risen, the European car industry has had to deal with decreasing domestic demand for cars. New passenger car registrations have not risen on a year-to-year basis since 2007, with demand falling by as much as 7.9% in 2008 and 5.6% in 2010. Recent statistical evidence suggests that the decrease in sales is far from over; compared to sales one year earlier, sales in September 2012 fell in France by 18%, in Italy by 26% and in Spain by 37%6. This plunge compounds a number of existing difficulties. For example, PSA lost EUR 819 million before tax in the first half of this year, while Renault had a negative cash flow of EUR 200 million7. Financial problems prompted some carmakers to dispose of parts of their European operations; Ford sold Jaguar Land Rover to India’s Tata Motors in 2008, and Volvo was sold to China’s Geely in 20108. Overcapacity, which has plagued many developed countries (as described in Section 2), is another by-product of Europe’s falling domestic demand. Fiat, PSA and Renault have estimated Europe’s oversupply at 20% as of March 20129. This, in turn, has taken a toll on factory operations: according to other estimates, approx. 30 of Europe’s 98 assembly plants are operating below 70% of their capacity10. The financial implications of these related problems are particularly dramatic for those carmakers with

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6 The Financial Times, France and Spain car sales slide further (01 October 2012)
7 The Financial Times, Peugeot and Renault line up a cavalcade, (25 September 2012)
8 Bloomberg, Geely Seals Takeover of Volvo From Ford (02 August 2010)
9 The Financial Times, Fiat chief calls for EU intervention (06 March 2012)
10 The Financial Times, Car industry rattles on old Europe’s roads (04 October 2012)
weak sales in the premium car segment and/or growing overseas markets, where demand for higher-end cars of European origin remains high.11

In addition to falling car sales, many European car manufacturers have had to grapple with a declining market share. As the graph below indicates, PSA Peugeot Citroen, Renault, Opel and Fiat each lost approx. 0.8 % of their share in the western European market in less than two years. Volkswagen, on the other hand, gained 1.3 % within the same time period, and South Korea’s Kia gained 0.5 %. Hyundai’s market share grew over the past two years by 0.4 %, extending its period of uninterrupted growth to 41 consecutive months as of July 2012.12 Significantly, the sales of Volkswagen Group, Kia, and Hyundai grew in the low-cost end of the market, which offers margins as high as 6 % — two to three times higher than in the sector as a whole.13 A number of car manufacturers are, however, losing their domestic markets. For example, new registrations of Peugeots and Renaults in France dropped by 20 % in September 2012, while year-on-year sales of Hyundai and Kia were up by 24 %.14

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11 This has been made apparent by the contrasting fortunes of high-end German car makers (Audi, BMW, Mercedes-Benz) and other European car makers (Fiat, Opel, PSA Peugeot Citroen, Renault)
12 Reuters, Analysis: Carmakers dampen EU free-trade drive (06 July 2012)
13 Renault Group cited in The Financial Times, Peugeot and Renault line up a cavalcade, (25 September 2012)
14 The Financial Times, France and Spain car sales slide further (01 October 2012)
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The European car industry is still a major employer.

The economic importance of the European car industry cannot be overlooked. The car sector directly employs 6.3% of Europe's manufacturing labour force — 2 million people — and another 3.9% — 1.2 million people — through its suppliers. Most of Europe's car assembly plants are concentrated in a handful of regions, such as Bavaria in Germany, Piedmont in Italy, western Slovakia and central Bohemia. The automotive industry is also the largest private investor in research and development (R&D) in Europe, having invested EUR 26 billion in innovation in 2011. The loss of these jobs and investments would have significant economic and political repercussions. Yet closing plants and laying off workers may be the only way for European carmakers to escape their current predicament, as the productivity of car plants within the EU varies greatly. For example, in 2009 Fiat's 22 000 workers in Italy produced 650 000 cars in five assembly plants, while 6 100 of their Polish counterparts produced 600 000 cars in a single Fiat plant in Tychy. Similarly, PSA Peugeot Citroen produced 1.27 million motor vehicles in 2010 in France, where the company employed approximately 104 465 employees (15 000 of them engaged in R&D); its Slovak plant produced more than 186 000 vehicles with only 3 000 employees. Faced with declining sales, poor financial results and overcapacity, PSA Peugeot Citroen announced earlier this year that it would make 8 000 workers redundant and close the Aulnay plant near Paris by 2014.

Source: ACEA data

15 Up to September 2012
16 The Financial Times, France and Spain car sales slide further (01 October 2012)
17 OICA for car production data; Autoevolution, Peugeot cuts 5,700 jobs in France for PSA France employment data; SARIO for PSA Slovakia employment data
18 BBC News, Peugeot Citroen plans 8,000 job cuts (12 July 2012)
Consolidation may be the way forward for many European car makers. Some industry insiders, including Fiat CEO Sergio Marchionne, have argued that this would help to address the overcapacity issue by shutting down underused plants and create savings by manufacturing cars on common platforms\textsuperscript{19}. In February 2012, Peugeot and Opel (GM) announced plans for a strategic alliance, which would enable each manufacturer to save close to EUR 1 billion per year. The partners are currently discussing deepening their ties to make even more substantial savings\textsuperscript{20}. Daimler is reportedly on its way to becoming the third member of Renault-Nissan alliance, while Fiat and Chrysler have also embarked on a strategic partnership, which has been described as a potential merger\textsuperscript{21}. While consolidating European car makers should increase their competitiveness and help address current financial difficulties,

\textsuperscript{19} The Financial Times, \textit{Carmakers must merge, says Fiat chief} (11 January 2012)
\textsuperscript{20} Reuters, \textit{GM and Peugeot weighting deeper tie-up: sources} (12 October 2012)
\textsuperscript{21} The Economist, \textit{Despite the troubles in past alliances, carmakers are embracing their rivals} (06 October 2012); Reuters, \textit{Fiat-Chrysler merger still on track despite lawsuit: CEO} (27 September 2012)
The EU automotive sector in a globalised market manufacturing jobs are likely to be lost in the process.

The European Commission has recently issued its CARS 2020 Action Plan ‘aimed at reinforcing this industry’s competitiveness and sustainability towards 2020’\textsuperscript{22}. The Plan advocates four concrete measures:

- promoting investment in advanced technologies and innovation,
- improving market conditions,
- supporting industry access to the global market,
- promoting investment in skills and training to accompany structural change and anticipate employment and skills needs.

The third pillar (concerning the global market) clearly involves targeting tariff and non-tariff barriers, as it promises ‘the conclusion of balanced trade deals’ and ‘intensifying the work on international harmonisation of vehicle requirements’. Industry response to this initiative has been lukewarm: the European Automobile Manufacturers’ Association (ACEA) Secretary-General Ivan Hodac called it ‘necessary but not sufficient’ and argued that the EU should also ‘explore ways to improve labour flexibility and support the affected workers and regions’\textsuperscript{23}.

\textsuperscript{22} European Commission, \textit{CARS 2020: a strong, competitive and sustainable European car industry} (08 November 2012)

\textsuperscript{23} ACEA, \textit{Press Release: European Automobile Manufacturers Call for EU Policy Automotive Industry to be Translated into Urgent Action} (08 November 2012)
In addition to employment, European carmakers provide a sizeable proportion of EU exports. As of 2011, the value of passenger car exports to countries outside the EU reached EUR 93.8 billion, a rise of 22.9% in comparison with the previous year. The EU is the world’s largest car exporter, and the industry’s export orientation is underscored by its positive and increasing trade balance, which reached EUR 69.6 billion in 2011, a one-year increase of 28.7%. These figures gain further significance when placed in a comparative perspective. Manufactured goods in general were responsible for around 80% of total EU exports in 2011, generating a trade surplus of EUR 264 billion. The car industry was thus responsible for more than one quarter of the surplus in trade of manufactured goods. Increasing car exports to emerging markets could help Europe’s carmakers to address the issue of falling domestic demand as well as their growing overcapacity problem in many EU plants. The tariff and non-tariff barriers that European car exporters face are therefore of crucial importance, both in countries that are already significant recipients of European car exports — such as the United States, China and Russia — and, more importantly, in those countries in which existing tariff and non-tariff barriers play a role in limiting the volume of European car exports.

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24 Eurostat
25 Ibid.
The European car industry is currently facing significant challenges:

In sum, the European car industry is currently facing significant challenges: falling domestic sales and overcapacity. Not all European carmakers have, however, been equally affected; Volkswagen and South Korean companies with assembly plants in Europe have, in fact, steadily increased their market share. On the other hand, PSA Peugeot Citroen, Renault, Opel and Fiat have experienced much greater structural and financial difficulties, as well as a declining market share. Industry consolidation has been suggested as a solution to their current woes; increased exports another.

Against this backdrop, and in order to understand the likely benefits of different approaches, the following sections will offer an analysis of various export markets and the various tariff and non-tariff barriers that European car producers face in these markets.
4. Export markets

Europe’s car export markets can be divided into two broad categories according to trade balance. Japan, South Korea and India are three important markets, with which EU’s trade balance in cars is negative — the result of the countries’ export performance and the trade barriers they have put in place. The EU maintains a trade surplus with other major countries, yet its market share varies. The EU is the leading exporter in Russia and China, second to Japan in the US, and far behind regional export powerhouses Brazil, Argentina and Indonesia. The premium car sector is responsible for the bulk of EU exports in most countries.

4.1. Trade deficit

4.1.1. Japan

The EU’s trade deficit in passenger cars with Japan is substantial but gradually decreasing, having fallen by 75% between 2008 and 2011 to USD 2.83 billion. Falling demand in Europe, the strong Japanese yen and the shift of production of Japanese cars to Europe were responsible for the drop of Japanese exports. EU car exports to Japan grew by one quarter within the same period, cementing the Union’s position as the leading car exporter worldwide.

Imports of foreign cars have increased in Japan, defying the more general and long-term Japanese trend of falling car sales. While only 1 in 20 cars in use in Japan in 2011 was of foreign origin (most of these European), the total number of European cars in Japan is relatively high; by comparison, only 3.9% of all cars in use within the EU are Japanese imports. The market share of foreign carmakers in Japan is relatively strong for ‘standard’ cars (15.5%), while negligible in the two thirds of the market occupied by small and ‘kei’ micro cars. High-end German carmakers command the majority of the Japanese foreign car market, and the market share of Europe’s struggling carmakers — Renault, Peugeot, Citroen and Fiat — remains insignificant: these four manufacturers together exported fewer cars into Japan in 2011 than did Audi.

European carmakers remain wary of the looming EU-Japan FTA, fearing that it would be used by Japanese carmakers to offset the losses incurred by falling domestic sales. ACEA has called for a level-playing field — the

26 UN Comtrade
27 Prof. Yorizumi Watanabe, European Parliament Workshop – Towards a Free Trade Agreement with Japan? (11 September 2012)
28 Out of 58.2 million cars in use in Japan in 2011, 29% were classified as ‘standard’, 40% as ‘small’ and 31% as ‘kei’ (JAMA data).
29 Audi’s exports in 2011 were 21,166 units. The total number of the four aforementioned carmakers was 18,225 units. Total imports into Japan in 2011 were 260,707 units.
30 The Financial Times, EU and Japan to start trade deal talks (29 November 2012)
4.1.2. South Korea

The EU’s trade deficit in passenger cars with South Korea halved between 2008 and 2011, dropping to USD 2.29 billion. EU exports nearly doubled, while imports from South Korea, especially in the more lucrative medium and large engines category, declined by over USD 1 billion. The most recent statistics confirm these trends.

The EU is the dominant car exporter to South Korea. Sales of imported cars have been on the rise in South Korea, growing from 5.2% of total sales in 2009 to 8.7% in 2011. This 72% increase represents a more rapid rate of growth than in Japan, where sales of foreign cars grew by 55.3% in the same span. As in Japan, sales of foreign cars in South Korea defied the domestic trend of falling sales. In general, the growth of car sales in South Korea levelled off in 2011 and fell by 7% on a year-to-year basis in 2012.

Further parallels exist between Japan and South Korea in terms of market share. In 2011, the high-end German carmakers Mercedes-Benz, BMW and Audi were responsible for more than one half of all sales of imported cars in South Korea. Struggling European carmakers have either no market presence — as is the case with Fiat — or an insignificant market share — as is the case with PSA Peugeot Citroën (2.5%).

The EU-South Korea Free Trade Agreement, which has been in force since 1 July 2011, is to eliminate the custom duty in medium and large cars by 2014 as well as the tariff on small cars by 2016. European car makers have been concerned about what they called 'asymmetrical trade flow relations': sales of South Korean cars have, in their view, risen in Europe in general. Believing that its market was particularly affected, France asked the European Commission to monitor car imports from South Korea. This request was rejected on the grounds of a lack of evidence that the increase in imports was concentrated in France. Moreover, the South

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31 ACEA, EU-Japan FTA: Tentative beginnings, uncertain gains (29 September 2012)
32 Korean car exports to the EU fell by 16.5% in September 2012 on a year-on-year basis while EU exports grew by over 20%; Korea Customs Service, Trade Statistics (September 2012)
33 Authors’ calculations based on KAIDA data
34 Authors’ calculations based on KAIDA and JAMA data
35 2012 data between up to August 2012; KAMA data
36 Hyundai sales in the EU were up by 12%, Kia sales by 25% in Q1 2012, while the EU car market was down by 8%; year-on-year imports to France grew by 50% in Jan-Feb 2012, sales of small South Korean cars grew by nearly 150% between January and June 2012. The Financial Times, Ford Europe hits at EU-Korea trade deal (01 May 2012); Embassy of France in Washington, European Commission, Car imports from South Korea factsheet France/EU-South-Korea FTA (03 August 2012)
37 The Wall Street Journal, EU Rejects Call to Monitor South Korean Auto Imports (22 October 2012)
Korean car manufacturer Hyundai maintained that there was no link with the free trade agreement since less than 12% of its more than 230,000 cars registered in Europe in the first half of 2012 were imported from Korea. 70% of Hyundai cars registered in Europe within this period were manufactured in its plants in the Czech Republic and Turkey.  

4.1.3. India

In relative terms, the EU’s USD 1.98 billion trade deficit in passenger cars with India dwarfs its deficits with Japan and South Korea. European car exports grew by mere USD 20 million between 2008 and 2011, while car imports from India increased within the same period by 150% to USD 2.15 billion. European car exports to India in 2011 were eight times lower than imports. India profited from a low 6.5% import tariff, a weak Indian rupee and the increasing local availability of compact cars by non-European manufacturers — Hyundai, Suzuki and Nissan. EU exports to India remain low, courtesy of high tariff barriers.

Sales of passenger cars in India doubled between 2005 and 2011 and are projected to grow to 6.73 million units by 2020, which will transform India into the second-largest car market in Asia after China in the not so distant future. The short-term outlook is, however, less positive, as the generalised economic slowdown, combined with increases in tariffs and financing costs, resulted in a 19% year-on-year decrease in output in August 2012. Predictions for this year’s growth in sales of passenger cars in India are 1-3%, down from a previous estimate of 9-11%. Given the substantial market access barriers in place, most European carmakers export completely knocked-down units, which are assembled locally and thereby subject to a substantially lower tariff. Europe’s carmakers are paying close attention to India. For example, one in five vehicles launched by Renault between May 2011 and December 2012 is designed principally for the Indian market. High-end carmakers are expected to benefit from the projected trebling in sales of luxurious vehicles in India by 2020.

The car sector has proven to be a contentious element in the EU-India FTA negotiations. India’s car sector has very little incentive to open up, as it benefits from low EU import tariffs and might well suffer from the removal of protective tariffs at home. European car manufacturers have called for

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38 Reuters, EU mulls French request for surveillance of South Korea car imports (06 August 2012)
39 The Wall Street Journal, Corporate News: India to Overtake Japan in Car Sales (15 March 2012)
40 The Financial Times, Indian car market suffers sharp slowdown (03 October 2012)
41 The Financial Times, Car sales rebound in India and China (09 November 2012)
42 The Financial Times, India: Renault makes up for lost time? (12 September 2011)
43 The Financial Times, Three-way race for India’s luxury market (28 August 2012)
4.2. Trade surplus

4.2.1. United States

With the onset of the country’s subprime mortgage crisis, the US car market suffered a significant decline. In a mere two years, the US went from being the largest market in the world, with 16.5 million units sold in 2007, to 10.6 million units in 2009. The country was overtaken by China one year later.\(^{45}\) The market has been gradually recovering since, with over 13 million units sold in 2011. The outlook for future growth is positive, as sales reached their highest number in four years in September 2012, up by 14.5% for the first nine months of the year in comparison with the previous year.\(^{46}\) Increasing fuel prices, prompting consumers to replace old vehicles with newer, more fuel-efficient models, have been identified as one of the principal causes of this growth in car sales. Sales of small cars increased by 50% on a year-on-year basis in September 2012, whereas sales of SUVs were down by 3.6%.\(^{47}\) Higher availability of low-interest credit and the improving US housing market have also boosted car sales.\(^{48}\) Some doubts remain about the market’s strength, given low consumer confidence levels and fears of a contagion of the deterioration of Europe’s car industry, but the outlook for the current year is generally positive.\(^{49}\)

The EU balance of trade in cars with the US reached USD 18.1 billion, down 12.4% from 2010, but up by a third from 2009, when EU exports hit their record low. EU car imports from the US grew by 57.6% between 2009 and 2011, contrary to the downturn in car sales within the EU. EU exports, valued at USD 24.7 billion in 2011, still lag behind their pre-crisis levels of USD 30.3 billion. The EU is the second-biggest car exporter to the US, ranked behind Japan, which exported USD 30.9 billion worth of cars into the US in 2011. The US demand for imported cars in the year up to September 2012 was 24%. Some European carmakers have been

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44 Examples include the reduction of India’s car imports duties to 30% in return for immediate duty-free access to the EU, with a possibility of introducing a fixed quota of cars on which a lowered 10% tariff would apply for a period of five years; The Financial Times, *Europe’s carmakers hit out at India trade deal* (29 January 2012); The Economic Times, *You may have to pay just 10% duty on Porsche and BMW; India in talks with EU to slash tariff* (30 July 2012)

45 WardsAuto data

46 The New York Times, *Auto Sales Are Highest In 4 Years* (02 October 2012)


48 Generally speaking, improving housing market tends to have a positive impact on consumer spending.

49 Reuters, *US new-car sales in August seen up as much as 20 percent* (04 September 2012)
particularly successful, with Volkswagen’s volume of exports to the US growing by 117 % within the same time period\textsuperscript{50}.

\subsection*{4.2.2. China}

The growth of China’s market for passenger cars has been unprecedented. The number of units sold more than doubled in three years, rising from 6.76 million in 2008 to 14.5 million in 2011. The market showed some signs of slowing down, with sales increasing by only 5.1 % between 2010 and 2011 due to the withdrawal of a 2009 government stimulus package, which favoured cars with smaller engine sizes, and the gradual tightening of credit policy by the central government\textsuperscript{51}. Car sales have risen over recent months, up by nearly 7 % year on year in October, with 12.57 million units sold in the year up to October 2012, spurred by recent fuel price cuts and the rush to buy a car before more Chinese cities introduce expected licence plate restrictions\textsuperscript{52}. These sales figures do not, however, reflect sales to end consumers, and inventories at car dealerships are reportedly rising. The single-digit growth that has recently characterised the Chinese car market is seen as signalling a period of adjustment, from hyper-growth towards a more sustainable growth, in line with the country’s GDP growth\textsuperscript{53}. The potential of China’s car market remains enormous, as its vehicle ownership rates remain relatively low: 58 units per 1 000 people, compared to 600 units per 1 000 in the G7 countries\textsuperscript{54}. Foreign brand ownership is high. Foreign brands are estimated to have accounted for 70.9 % of car sales in 2011, up 1.8 % from 2010\textsuperscript{55}. Moreover, while the Chinese car market grew by approximately 115 % between 2008 and 2011, imports from the triad countries grew by almost 190 % within the same period\textsuperscript{56}. EU car exports to China increased by 223 %, from USD 6.8 billion in 2008 to USD21.9 billion in 2011, exceeding exports from other major car-exporting countries by USD 6.9 billion. Total EU exports of goods to China reached EUR 136.2 billion in 2011, meaning that the car sector provided approximately 12 % the year’s goods exports to China. European luxury-car manufacturers have been particularly successful in China. For example, BMW recorded a 33.5 % increase between January and September 2012, well ahead of the market average of 7 %, and the company’s Chinese sales have accounted for almost 50 % of its EUR 18 billion improvement in revenues since 2009\textsuperscript{57}.

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4.2.3. Russia

The Russian car market collapsed in the aftermath of the financial crisis, with sales falling between 2008 and 2009 by over 1.4 million units, to 1.47 million units. The market has since then steadily improved, with sales figures as high as 2.65 million in 2011. Sales are expected to grow by 12.4% this year, exceeding 2008 sales. If this rate of growth were to continue, Russia would become the largest car market in Europe by 2016, exceeding even Germany (currently the largest market in Europe). Total industry sales in Russia were estimated at USD 65 billion in 2011, up by 55% from the previous year. Economic recovery (linked to high oil prices) and government stimulus measures—such as the extension of a car scrapping scheme until the end of 2010—and the greater availability of loans have been identified as the key drivers of this growth. Russia’s vehicle density of 250 units per 1,000 people is lower than that of many key European markets, offering significant potential for growth.

Imports in 2011 were estimated at 34% of total car sales. Cars and other vehicles constitute the main EU export to Russia, and European export volume reached USD 8.9 billion in 2011. The EU was the leading car exporter to Russia in 2011, exporting USD 1.8 billion more than Japan, although the EU’s 2011 volume was only 68% of its 2008 figure, nearly USD 13 billion. Although Russia entered the WTO in August 2012, EU exporters are not likely to benefit in any significant way from the gradual decrease of import duties that will accompany Russia’s accession, as the introduction of a car recycling fee by the Russian government will offset the lowering of import duties. According to an initial analysis from the Commission, the recycling fee will result in a decrease of more than EUR 1 billion per year in the value of the EU’s export of vehicles to Russia.

Since 2005 Russia has also introduced an aggressive localisation policy measures in the automotive sector. This principally consists of an “industrial assembly” regime, which imposes local content requirements that gradually increase to 60% by 2016, as well as a minimum capacity of 300,000 units per year for entities establishing new production capacities and 350,000 units per year for entities modernising existing capacities. Other requirements include, for example, the establishment or modernisation of R&D centres in Russia and reaching a minimum average annual level of production localisation in the Russian Federation. These developments will only compound the existing overcapacity problem in

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58 Ernst & Young, An overview of the Russian and CIS automotive industry (February 2012)
59 Russia Today, Russia in high gear to become top car market in Europe (24 September 2012)
60 Ernst & Young, An overview of the Russian and CIS automotive industry (February 2012)
61 Ibid.
62 The Moscow Times, After WTO, Carmakers Still Protected (30 August 2012)
Policy Department, Directorate-General for External Policies

4.2.4. Brazil

The EU managed to reverse its trade deficit in cars with Brazil, going from a deficit of USD 290 million in 2008 to a USD 1.62 billion surplus in 2011. EU exports nearly doubled, while imports from Brazil declined by 90% due to the strong Brazilian currency, the real, and falling demand in Europe.

European car exporters were able to capitalise on Brazil's surging demand for imported cars, which grew between 2008 and 2011 by 153%, reaching nearly 580,000 units. Car sales in Brazil increased between 2008 and 2010 by 20.6% to 2.64 million units. Although growth stalled in 2011, the outlook for the Brazilian car market remains positive; borrowing costs have decreased, and the government recently cut excise taxes, resulting in an 18.9% increase in car registrations in July 2012 compared to one year previous. The rate of growth of imported cars has, however, declined, from 26% in 2011 to mere 5.2% in August 2012. This decline is a direct consequence of an increased number of protectionist measures aimed at curbing the rising number of imports, considered threatening to Brazil's domestic manufacturers and industrialisation efforts. For example, in March 2012, Brazil imposed a quota on car imports from Mexico, which had risen by 70% in 2011. Previously, in December 2011, a tax on cars with less than 65% local content had been increased by 30% to 55% allegedly to safeguard against imports from China, which had risen five-fold in 2011. The scheme was modified in October 2012, becoming the Inovar-auto program, but it retains its discriminatory character towards imports and builds upon tax exemption incentives for the localisation of production, R&D and engineering. This may have a particularly negative effect on EU car components exports to Brazil.

Fiat and Volkswagen sell two in five cars in Brazil, but sales are forecast to

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64 The Financial Times, VW hit by Europe slowdown (24 October 2012)
65 ANFAVEA data
66 The Financial Times, Tax breaks boost Brazilian car production (06 August 2012)
67 ANFAVEA data
68 Reuters, Mexico bows to Brazilian pressure on auto exports (15 March 2012)
69 The Economist, Brazil’s trade policy: Seeking protectionism (14 January 2012)
drop by 8.3 % and 8.4 % respectively for each manufacturer in 2013, when Brazil’s local car production capacity will receive a major boost from new factories for Hyundai, Chery and JAC Motor\textsuperscript{70}. Other European carmakers, including BMW and Mercedes-Benz, are reportedly interested in investing in Brazil in order to circumvent trade barriers and profit from the growing car market\textsuperscript{71}.

### 4.2.5. Argentina

Argentina’s passenger car market contracted in the immediate aftermath of the world financial crisis, dropping to around 453 000 units in 2009, but went on to make a strong recovery, with 673 900 units sold in 2011\textsuperscript{72}. The increase in supply was met by growing domestic production, which reached record levels of around 840 000 cars in 2011, and increased imports from Brazil, which increased by 60 % to USD 3.62 billion between 2008 and 2011\textsuperscript{73}. EU car exporters largely did not profit from this recovery to the same extent as their Brazilian counterparts did: EU exports grew by only 23 % within the three-year period, although they declined by USD 45 million between 2010 and 2011. In 2011, EU exports to Brazil were valued at USD 480 million.

The Argentinean car industry is showing signs of slowing down. Car production decreased by 21 % on a year-to-year basis up to September 2012. This was mainly due to the depreciation of Brazil’s currency, which rendered Argentinean cars in Brazil — Argentina’s principal car export market — more expensive\textsuperscript{74}. Moreover, Argentina’s has faced an own economic slowdown, with GDP growth halving to 3.4 % in 2012 and placing capital at risk of flight\textsuperscript{75}. Car sales, as a result, have fallen by 9.6 % in the year up to October 2012. The Argentinean government has tried to partially shield its industry from imports and has renegotiated its automotive accord with Mexico, which has led car imports to decrease by 16.6 %\textsuperscript{76}.

### 4.2.6. Indonesia

Indonesia, the fourth most populous country in the world, has car ownership rates as low as 4 % and thus promises an enormous potential for future growth\textsuperscript{77}. Indonesia’s economy, fuelled by rising domestic

\textsuperscript{70} Bloomberg, \textit{Fiat Faces Challenge as Hyundai Threatens Profit} (22 October 2012)
\textsuperscript{71} The Financial Times, \textit{BMW eyes plans for Brazil factory} (19 October 2012); The Wall Street Journal, \textit{Mercedes-Benz May Decide on New Brazil Factory by Year End} (22 October 2012)
\textsuperscript{72} ADEFA data
\textsuperscript{73} ADEFA data; UNCTAD
\textsuperscript{74} The Financial Times, \textit{Argentine autos: bumpy road ahead} (07 November 2011)
\textsuperscript{75} Bloomberg, \textit{Argentine Budget Sees 3.4% GDP Growth in 2012, 4.4% in 2013} (20 September 2012)
\textsuperscript{76} The Financial Times, \textit{Auto fight: Argentina wants a piece of Mexico too} (21 March 2012), ADEFA data
\textsuperscript{77} The Economist, \textit{Indonesia’s car market: Stuck in the fifth gear} (01 September 2012)
consumption, grew by 6.5% in 2011, with GDP per capita reaching USD 3 500 — a threshold considered the ‘take-off point’ for car sales. Sales of all motor vehicles grew by 17% in 2011, contrasting with falling sales in other ASEAN countries. Sales of motor vehicles in Indonesia are projected to reach 1.06 million units this year and double to 2 million units by 2018. Indonesia is expected to become the biggest car market in Southeast Asia.

EU car exports to Indonesia grew by 44% between 2008 and 2011, reaching USD 133.5 million in 2011. This figure was only about one quarter of Japanese car exports to Indonesia, and only slightly higher than that of South Korean exports, which increased eight-fold within the same time period. Thailand, used as a regional car-manufacturing hub by Japanese carmakers, remains the most significant car exporter into Indonesia, with exports higher than those of all other countries combined.

Japanese carmakers control over 90% of the Indonesian car market. They will likely maintain their leading position given their plans to USD 2 billion by the end of this year to expand their manufacturing capacity in Indonesia. General Motors is investing USD 150 million to reactivate a defunct Indonesian plant in a bid to recapture a share of the growing Indonesian market. European carmakers, on the other hand, have been much less active. Peugeot was reportedly interested in investing USD 150 million in Indonesia in 2011, but its plans have been delayed by the company’s on-going financial difficulties, and there has been no official confirmation of this investment.

5. Tariff and non-tariff barriers

As the above survey of various markets demonstrates, European car exporters maintain a leading position in a high number of geographically diverse markets, with luxury cars constituting the key segment in the majority of these markets. Market openness, however, remains an issue. EU car exports to developing markets, such as India and Indonesia, and to certain developed markets, such as Japan and South Korea, remain low and/or restricted to more expensive cars only. Tariff and non-tariff barriers in many countries have had a major impact on the overall volume of EU car exports, as well as on segmentation, which makes EU exports of standard and lower-end cars less competitive.

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78 The Financial Times, Boom time for Indonesia’s car industry (10 October 2012)
79 ASEAN Automotive Federation.
80 Reuters, Indonesia Sept car sales jump back to near record levels (15 October 2012); The Financial Times, Boom time for Indonesia’s car industry (10 October 2012)
81 The Financial Times, Boom time for Indonesia’s car industry (10 October 2012)
82 The Jakarta Globe, GM, Peugeot to Revive Plants for Production (12 August 2011)
83 BSD, Indonesia Trade & Investment News 06/12 (June 2012)
5.1. Tariff barriers

Import duties faced by European car exports in developed car markets are relatively low, ranging from 0% in Japan to 5.6% in South Korea and 10% in the US. The EU import tariff itself is 10% or 6.5%, with the lower rate applying to developing countries. On the other hand, a number of growing automotive markets, including those listed below, apply import tariffs that vary from 25% in Russia and China to 75% in India and even 83% in Vietnam. India is a very specific case, as its automotive industry has clearly profited from the low EU duty applied to Indian exports; the country exports a high number of cars to the EU, as well as to other countries.

![Figure 3:](image)

Automotive peak tariffs in selected markets, November 2012

<table>
<thead>
<tr>
<th>Country</th>
<th>Tariff</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>25%</td>
</tr>
<tr>
<td>India</td>
<td>75%</td>
</tr>
<tr>
<td>Argentina</td>
<td>35%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>30%</td>
</tr>
<tr>
<td>Russia</td>
<td>25%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>50%</td>
</tr>
<tr>
<td>Brazil</td>
<td>35%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>83%</td>
</tr>
</tbody>
</table>

The European Commission has repeatedly promised to address these tariff imbalances in trade negotiations with its partners by concluding ‘balanced trade deals’, as reiterated in the CARS 2020 Action Plan. European car manufacturers have, for their part, frequently called for securing a level playing field in any future trade agreements, such as the FTA with India currently being negotiated.

5.2. Non-tariff barriers

Non-tariff barriers (NTBs) can, in many cases, pose even more formidable obstacle to car exports than tariff barriers. This is certainly the case with Japan and South Korea, where EU car exporters face low — and sometimes no — import duties, while their export volume remains relatively low. As far as developing markets are concerned, NTBs tend to significantly increase the price of imported cars, which are already expensive and attract high import duties.

NTBs take many differing forms, which makes them hard to fully eliminate. Technical regulations are among the most common NTBs. Their effect can be particularly strong due to the growing gap between EU regulations and foreign regulations, which often results in significant costs for EU car manufacturers. The EU-South Korea FTA, which entered into force in July 2011, includes ambitious provisions that would make a number of EU technical requirements apply to the Korean market. In spite of this, ACEA, which represents European manufacturers, reports and lists a number of.

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84 More than 30% if the recycling fee is taken into account.
85 European Commission, CARS 2020: a strong, competitive and sustainable European car industry (08 November 2012)
86 The Financial Times, Europe’s carmakers hit out at India trade deal (29 January 2012)
regulatory issues in South Korea as 'pending'. Examples include test procedures, conditions and criteria for certification, post-market surveillance and vehicle width. Other countries — most notably Indonesia — are also introducing their own national standards. According to the provisions of the Indonesian National Standard (SNI), SNI certifications will be required for car components (such as braking systems) and for completely built cars (such as tyre and windscreens). This trend towards greater local regulations is worrying for European carmakers, which control only a small fraction of the market, as 'SNI certification and testing proved to be lengthy and costly'.

Homologation procedures, closely related to technical regulations, can be equally thorny. For example, motor vehicles imported into China 'are subject to more than one type-approval/homologation requirement' by different, uncoordinated regulators. Moreover, under the provisions of the 2002 China Compulsory Certification system, each automotive product and component that has been type-approved in Europe must be re-tested in Chinese laboratories, imposing a further burden on importers.

Tax structures in certain countries may also discourage customers from purchasing imported cars. Examples of such structures include the luxury car tax in Indonesia and the Brazilian industrial tax (IPI). The IPI, which was initially re-introduced in December 2011 and extended to 2013-2017 in April 2012, is as high as 30%. The tax applies to motor vehicles unless their manufacturers comply with at least three out of four prescribed rules, for example adhering to content requirements (i.e. meeting an onshore-manufacturing threshold) or making R&D investments in Brazil.

Other NTBs vary widely. For example, the recycling fee on imported cars to be introduced in Russia will more than offset the planned lowering of tariffs. An importer declaration system in Argentina requires that imports be reported in advance. In China, draft public procurement rules for official party and government cars only feature vehicles from Chinese carmakers. Finally, in Japan, owners of Japanese kei cars — domestically manufactured micro-cars with a market share of over 30% — enjoy...

87 ACEA, EU-South Korea FTA: Resolution of Remaining Issues (20/10/2011); European Commission, Report of the meeting of the Market Access Working Group on Cars and Car parts and Market Access Working Group on Tyres (09 February 2012)
88 European Business Chamber of Commerce in Indonesia, Automotive Position Paper 2012 (27 July 2012)
90 Ibid.
91 European Commission, The Ninth Report on Potentially Trade Restrictive Measures (06 June 2012)
92 Ibid.; ACEA, EU-Japan FTA: Tentative beginnings, uncertain gains (29 September 2012)
93 Hosuk Lee-Makiyama, FTAs and the crisis in the European car industry (2012)
94 European Commission, CARS 21 High Level Group – Final Report (06 June 2012)
financial benefits. It has even been remarked that low market penetration by foreign carmakers can be an NTB in itself, creating a vicious circle. The total cost of owning a foreign car in Japan, for example, has been calculated at 30% more than that of comparable domestic models, purely due to the low availability of spare parts, diagnostic equipment and technical expertise. In such conditions, customers opt for domestically manufactured models, especially in the lower-end segments of the market, where cost is a primary consideration.

The strategy of the European Commission for removing NTBs is centred on facilitating worldwide acceptance of technical requirements and conformity assessment procedures, defined by the UNECE 1958 Agreement. FTAs are seen as useful tools for ensuring legislative equivalence, but they might not always accomplish the goal of removing NTBs. This was, for example, the case of the EU-South Korea FTA. Bilateral discussions, such as the EU-China Dialogue, may be of some help. Yet any successful elimination of NTBs can easily be reversed with the introduction of new NTBs. The range of possible NTBs is so broad that they pose an ongoing threat to future market access in any car export destination.

6. Conclusion

The global automotive industry has been affected by two significant developments in the past decade. The first was short-term, as global sales and production numbers temporarily dropped following the onset of the world financial crisis. The industry has, however, since recovered, and its current production levels exceed those of the pre-crisis era. The second development, on the other hand, is ongoing. Both sales and production have been shifting from the countries of the triad (the EU, US and Japan) to developing markets. Demand for passenger cars in countries such as China and India has soared. Although these markets have experienced short-term fluctuations in demand, their long-term outlook is quite positive.

The EU, the world’s leading car exporter, has been able to capitalise on this shift. Nearly every fifth car exported from the EU is destined for China. Passenger cars are responsible for a sizeable portion of EU exports of manufactured goods to the world’s second largest economy.

At the same time, many European carmakers are experiencing major financial and structural difficulties caused by stagnating domestic markets. A number of carmakers have suffered losses at home, within the very market segment that was traditionally one of their strongpoints. Among sales of small cars in France, for example, the market share of French brands has fallen, unlike that of their South Korean counterparts. The impact on struggling carmakers has been severe, as confirmed by their financial results and plans to lay off workers and close plants.

Overcapacity has often been cited as the principal cause of the current predicament. Addressing this issue, however, is no simple matter, and the
Increasing the levels of car exports appears to be the only plausible solution to Europe’s overcapacity problem. Given this context, increasing the levels of car exports appears to be the only plausible solution to addressing the issue of overcapacity in the short-run.

Our analysis of numerous important export markets has demonstrated that there is scope for such an increase. The EU, despite being the world’s leading car exporter, has only managed to incrementally reduce its trade deficit with other major car exporters, namely Japan, South Korea and — particularly — India. Foreign car ownership rates in Japan and South Korea remain low. India is adamantly shielding its domestic market from exports, while becoming an ever-more productive car exporter in its own right. Those countries with which the EU maintains a trade surplus are either still growing (as is the case for China, Brazil and Indonesia) or gradually recovering (the US). Russia’s recovery has also been significant, as the country is poised to become the biggest car market in Europe, perhaps as early as this year.

Tariff and non-tariff barriers, however, present a significant impediment to possible increases in the volume and segmentation of EU exports to these markets. Lower import duties — which the EU has vowed to secure by concluding FTAs — merely offer a partial solution, as countries tend to protect their domestic automotive industries and/or force carmakers to open plants at home. Non-trade barriers are both difficult to remove and easy to introduce, and they tend to offset any gains in the removal of trade barriers. More than a year has passed since the EU-South Korea FTA entered into force, for example, and European carmakers still voice their concerns about South Korean NTBs. The EU’s car exports to Russia have not benefited from Russia’s WTO membership (and the resulting 10% reduction in car import duties) because a new car recycling fee applied to imported vehicles will ensure that these cars remain as expensive as before. Examples of NTBs vary, but they all share an ease of implementation. Ensuring proper market openness to car exports will therefore remain a major challenge for the EU for many years to come.