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China’s tariff timing detracts from impact

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For those vehicle manufacturers that have already invested heavily in local production, a cut in import tariffs could eat away at their competitive advantage. By Megan Lampinen

The world’s largest vehicle market is taking further steps to open up its automotive industry. In April the focus was joint venture ownership; now it turns to trade policy. China has long protected its local manufacturers with steep vehicle import tariffs, which currently stand at 25%. As of 1 July that will drop to 15%. At the same time, tariffs on imported automotive components will drop to a flat rate of 6% – at the moment their tax rate ranges from 6% to 25% depending on category. These changes could make a big difference for both consumers and manufacturers, but some argue that the timing of the move detracts considerably from its overall impact.

For shoppers, the lower import tariff could mean a larger selection of more affordable models. “This decision to cut tariffs on car imports will further open and intensify competition in the Chinese autos market by giving foreign automakers a better chance of competing on cost with local manufacturers,” observed analysts at BMI Research. Already the likes of Toyota, BMW and Porsche have stated that they would re-examine their retail pricing following the government’s announcement.

For brands, it’s a mixed bag. Most industry watchers agree that it will give foreign OEMs a better chance to compete on costs with local players. The luxury players should feel the biggest benefit, as this segment has been taking a growing share of the total import figure. Neil Wang, Greater China President, Frost & Sullivan (F&S), specifically pinpoints Mercedes-Benz, Audi, BMW, Porsche and Tesla as beneficiaries.

Wijaya Ng, Head of Greater China, Ipsos Business Consulting, also sees considerable benefits for the luxury players, particularly those with larger engine capacities (above 3.0-litres). However, this is a relatively small segment, accounting for just 7% of China’s total vehicle imports last year. German brands in general are among the most popular imports, accounting for about one-third of China’s total vehicle imports last year. The US and Japan are close behind, at 22% and 20%, respectively. Luxury models from these regions should see a real benefit from the policy change.

On the other hand, the gains for joint venture brands are likely to be limited. These companies have already invested heavily over the years in local partners and local production operations. In fact, this tariff cut could eat away at their competitive advantage. Wang warns that the narrowed price gap could force JVs “to make strategy adjustment by enhancing production efficiency, shifting their development focus towards electrification or developing more connected and intelligent vehicles, etc.”

For Ng, the policy revision may improve foreign brands' margin but may not be sufficient to overhaul their existing or planned China JV strategy. "Tariffs only account for one part of the comprehensive tax in China for imported vehicles," he noted. While the tariff drops to 15%, VAT will only dip from 17% to 16% with consumption tax remaining at the same level.

Last year, imported models across all segments accounted for just 5% of China's total vehicle sales. BMI is forecasting a jump in this figure moving forward. At the same time, though, the reduction in component tariffs could bolster local production. "We may start to see increased usage of imported parts in local assembly to further improve the performance of vehicles, both as a differentiator between competing brands, as well as to close the gap with imported counterparts," Ng told *Automotive World*.

Similarly, BMI predicts that "this will provide an additional incentive for automakers to produce domestically following the government's decision to lift caps on foreign ownership of domestic automotive ventures in April." Since 1994, foreign vehicle manufacturers have been limited to owning no more than 50% in any local venture. Like the hefty import tax, this was designed to protect local players. For manufacturers of electric vehicles (EVs) and plug-in hybrid models, the JV ownership cap disappears later this year. They take effect for commercial vehicle companies in 2020 and for everyone else in 2022.