BRITISH BRANDS GROUP

Branding for Brexit

Assessing the climate for brands in the United Kingdom as a result of the Brexit referendum

The UK has now served its Article 50 notice. As outlined by Prime Minister May in January 2017, Britain intends to leave the single market and the Customs Union, while securing "the best deal" for an-outwardly facing Britain. New free trade arrangements will be put in place between the UK and the (post Brexit) EU, as well as with third countries. The UK aims to achieve special arrangements to maintain the Common Travel Area on the island of Ireland, while protecting the integrity of the immigration system, implying no hard border between N. Ireland and the Republic.

There remains a high degree of uncertainty about how far and whether the UK will be able to achieve Prime Minister May's stated objectives, about the timescales within which any trade deals will be possible and about any interim regime between Brexit and new deals. This uncertainty presents significant challenges. It could be as costly and difficult to prepare for a short interim period as it would be for a decade. The fact that the Government has since called an election in June, in the hopes of increasing its majority, in the short term only adds to that uncertainty.

At a time of uncertainty, there is real opportunity for brands to be seen as beacons of stability, trust and consistency if they align their communication and reputation management with consumer sentiment. There are also significant opportunities to demonstrate commitment to the UK, to UK jobs and to UK consumers.

Brexit and brands

Within a few months of the Brexit referendum, Unilever and Tesco were in a very public "Marmitegate" standoff over Unilever's reported attempts to secure a 10% across the board price increase due to the falling pound, countered by Tesco's "consumer champion" response. Toblerone was another brand to hit the headlines within a few months of the referendum as its size shrank and its familiar and much-loved shape changed because, its makers claimed, the cost of ingredients rose due to Brexit.

Consumer brands are likely to continue to operate as bellwethers for Brexit's impact, as journalists and commentators naturally seize on them as everyday products with which many are familiar. Brand owners will need to be very focused on reputational effects of steps they take, be that changes to their products, price increases, job cuts or changes to where their products are made.

Exchange rate volatility and the potential for increased tariff and non-tariff barriers affecting products and pricing are further reasons why brands will need to communicate openly with consumers about changes affecting products, pricing and jobs. This will require coherent strategies that consumers do not see as simply "blaming Brexit" or, worse, exploiting the
situation, but which do ensure consumer expectation is calibrated to a "new normal" when it comes to product availability and pricing.

Trusted brands can provide a reassuring consistency and continuity if they can anticipate and react to consumer sentiment as it evolves. Brands with a strong UK heritage may be able to emphasise it and foreign brands may be able to gain consumer trust by demonstrating their continued commitment to consumers and jobs in the UK. Even when pricing is under pressure, brands may be able to reinforce their image as consumer champions by careful communication around what they are doing to secure continued value for their consumers. As the UK forges new links with third countries, there may be new opportunities for British brands to develop new markets.

The spectre of price rises and trade barriers

*Exchange rate volatility*

The Brexit vote immediately caused a significant fall in sterling, causing it at one point to hit a 30-year low against the dollar. Prime Minster May's January 2017 twelve-point outline of her negotiating objectives caused a re-bound, but continued exchange rate volatility is likely as the contours of the UK's future trade relations evolve.

Currency market volatility will continue to affect brands which use foreign components, foreign raw materials or foreign processors. Many currency hedging arrangements and price commitments for imports put in place before the referendum have already expired and new arrangements are likely to be more difficult and more costly to put in place.

Consumer groups like *Which?* have criticised retailers and manufacturers for quietly re-engineering products to limit the effect of price rises on consumers, by making items smaller, using smaller packets and/or using cheaper raw materials for the same product, saying this amounts to a "sneaky way of raising prices".

Brands which react thoughtfully and communicate effectively around steps they are taking to reduce the impact on consumers and on jobs are more likely to weather volatility arising from volatile cost bases. In order to avoid reputational damage, brand suppliers will need to demonstrate their commitment by being transparent with consumers about the causes of price and product changes and how they are managing those that relate to Brexit. Consumer goods companies should be especially alert to retailers trying to position themselves as consumer champions at the expense of their suppliers.

*Tariff barriers*

Currently, because of the UK's membership of the single market and customs union, UK businesses have been able to import products, raw materials and components from the EU without any tariffs. Following Brexit, if no free trade agreement has been agreed between the UK and the EU, then the UK would be obliged to apply tariffs on all imports from the EU at the rates the UK applies on imports under its WTO commitments. This will almost certainly lead to increases in prices to consumers, although the impact will vary materially between sectors and categories. Tariffs on exports may also reduce or negate any competitive advantage achieved from falls in sterling.
Producers affected by increased costs from tariff barriers will need to react thoughtfully and communicate effectively around steps they take to contain price rises, including looking at whether costs can be saved by changing supply chain. In some areas, this may present significant opportunities for UK suppliers of ingredients, components, or processing services.

**Non tariff barriers**

In addition to the direct financial impact of tariffs, absent agreed free trade terms which avoid this, exit from the EU will lead to the introduction of "non-tariff barriers" on imports from (and exports to) the EU, which have not applied during the period of the UK's membership of the single market and Customs Union. Businesses will need to address these non-tariff barriers.

A non-tariff barrier refers to any measure that increases the cost of trade, but which does not take the form of a tariff. Some non-tariff barriers are bureaucratic – for example the additional cost of undergoing customs procedures for one day has been reported as equivalent to an additional tariff of between 0.6% and 2.3% of the value of a product. It also covers behind-the-border barriers, which are mostly regulatory measures, especially with regards to chemicals and food. These can reflect a genuine public interest, or protectionism, or both. They can be seen as "red tape" or – alternatively – as ways of opening up export markets for goods which meet minimum standards.

Changes in non-tariff barriers may shift consumer perceptions and may over time change the competitive landscape within categories, with implications for brand reputations and consumer understanding. In the current theme that Britain is "open for business", it seems relatively unlikely that the UK will introduce new protectionist measures unilaterally but brands will need to monitor, react to and communicate around changes in consumer perception and the competitive landscape.

**Supply chains and distribution networks**

Many UK companies have supply chains that cross EU boundaries. The imposition of tariff and non-tariff barriers will impact the ease of producing products and getting them to market. This may lead to some businesses reorganising their supply chains to minimise costs and to offshoring some activities currently handled in the UK to avoid trade barriers for exports.

There is an opportunity for UK suppliers to capture new business based on a more favourable cost benefit analysis of retaining production in the UK, with the added potential benefit of easier brand control and aligning the brand to a strong commitment to the UK. Conversely, exporters incentivised to move jobs overseas will need to consider brand reputation impacts and how the move is communicated.

Brexit will have particular impact on the UK’s only land border with the EU (Ireland). Managing Brexit-related issues arising across this border will be particularly complex and is likely to require careful and sensitive reputation management.

There will also potentially be sensitivities around Scotland, in view of the likelihood of a second independence referendum in future.
Workforce

Prime Minister May is steadfastly refusing to guarantee the rights of non-UK EU citizens to remain in the UK until reciprocal guarantees are agreed for UK citizens living in other EU countries. Additionally, what “taking back control” of immigration will mean in practice for new migrants and employers seeking workers remains unclear. Against the background of immigration being a key factor in the outcome of the Brexit referendum, branded companies will need to be very sensitive to issues relating to their workforce. This will include access to appropriate talent and workforce not readily available in the UK, and reputational impact associated with any restructuring that may take away UK jobs.

Restructurings to minimise tax impacts of Brexit

The tax position of multinationals with UK operations is likely to change materially on Brexit. UK-headquartered multinationals will be determining the size of the impact of likely liability to pay withholding tax on dividends from subsidiaries and, if it is material, thinking about contingency plans, for example accelerating profit distributions, restructuring the way profit is distributed within the group, or maybe even restructuring the group itself to avoid discrimination based on foreign ownership.

Although the Government has suggested that the UK will become a favourable tax environment, there has been strong reaction to this from EU spokespersons and popular sentiment in the UK and elsewhere is increasingly opposed to businesses not paying a fair share of tax at the point at which it is earned. In a climate which is increasingly hostile to arrangements designed solely to avoid tax and where there may be increased scrutiny of practices that may potentially damage the wealth of the UK, brands will need to be particularly sensitive to the reputational impact of tax-driven changes.

Exports: EU Market Access and a Free Trading Britain

Following Prime Minister May's January announcements, the most likely avenue is that the UK will try to negotiate a deep and comprehensive Free Trade Agreement (FTA) or Association Agreement, or perhaps a series of agreements covering key areas of activity, with the EU. If that is not possible, then the UK will default to WTO rules.

Trade deals are bespoke and typically designed by sector. Given the current complex interrelationships, any future UK/EU trade deal is likely to be unprecedented in scope and complexity. Businesses should continue to feed their key concerns and practical suggestions to Government either directly or via trade associations.

Because of the uncertainty around future trade deals, it will be critical to monitor the situation and communicate openly and effectively with key stakeholders. If the UK does leave the Customs Union, as foreshadowed by Prime Minister May, or otherwise agrees freedom to enter into FTAs with third countries, then there will clearly be opportunities and risks for UK branded suppliers. The opportunities are obvious – tariff free (or reduced tariff) access to sell products in new markets and, potentially reduced costs of imports and imported raw materials for goods made in the UK. Tate & Lye's executives, for example, informed the company's employees before the referendum that they thought the company would be better off outside of the EU if the UK could agree lower tariffs on the raw sugar cane it imports to be refined in the
UK. Some brands, however, will face lower cost competition entering the UK market – for example, imported dairy and chocolate products have historically been subject to high tariffs when entering from non-EU/EEA countries.

Protecting brands, innovation and consumers

During the UK's membership of the EU, its laws on intellectual property and consumer protection against misleading practices have been fundamentally changed. As well as extensive harmonisation of national rights, "unitary rights" (which are single rights covering the whole EU such as the EU trade mark and EU designs) reflect and promote the concept of the EU as a single market.

The proposed "Great Repeal Bill" will give the UK time to work out whether it wishes to stay assimilated in terms of the scope of harmonised protection under national law. But, unless the UK accepts, contrary to Prime Minister May's stated position, the continued jurisdiction of the EU Court of Justice, it will need to address how businesses who protect their brands and consumers in the UK via unitary rights will remain protected in a post-Brexit UK. The likely solution will be some form of transformation of the protection from EU unitary rights into UK national rights, meaning that equivalent protection is preserved.

There are some wider policy questions that need to be addressed. Of particular interest for brands are:

1. *Protection for trade dress.* On Brexit, one of the available legal bases for protecting trade dress, EU unregistered design right, will be lost. Although the UK has its own national unregistered design right, it does not apply to colours and surface decoration (as the current EU right does), the elements that are commonly copied features of packaging. The current UK regime for protecting trade dress is already perceived by many as inadequate, as was acknowledged in the 2006 Gowers Review of Intellectual Property. Brexit provides an opportunity to reassess how legal protection of brands and consumers can be better aligned to promote innovation, reputation and brand trust, without affecting the ability of competitors to compete fairly.

2. *Geographical Indications, Protected Designations of Origin etc.* Since the UK joined the EU, there has been an increased focus on provenance of products, especially in the food and drinks sectors. EU protection for Geographical Indications and Protected Designations of Origin has no fully equivalent UK system, so both UK and non-UK indications of provenance and type risk losing protection on Brexit. Providing continued protection for EU rights holders in the UK is likely to have a political value. Bodies such as the Scotch Whisky Association could play a leading role in steering policy on this.

3. *Parallel imports.* Current EU law and practice reflect the single market, i.e. once a product is put on the market anywhere in the EEA the brand owner has limited ability to object to resale anywhere else in the EEA. Conversely, a brand owner may exercise its rights to stop importation of parallel imports from outside the EEA which were not intended for European markets, as well as products to whose sale it has never consented (e.g. unauthorised manufacturing overruns). If the UK leaves the single market, the logic behind "EEA exhaustion" will likely fall away. If the UK defaults to "international
exhaustion", this may challenge the efficiency of using common branding for products which are locally tailored to different markets. It may also raise problems of brand consistency, quality control of supply chains, greater difficulties in dealing with counterfeits and unauthorised over-runs, challenges to selective distribution arrangements and difficulties with consumer guarantees and after-sales support.

Regulatory landscape

There is uncertainty over how the UK's laws will be affected in the longer term by Brexit and will inevitably be a long debate over which "EU laws" are kept and which are repealed. There is an opportunity for the UK to "start again" in areas of regulation where there are concerns or criticisms over onerous regulatory burdens, particularly for SMEs.

Some sub-sectors may seek an opportunity for greater or further self-regulation in terms of advertising and consumer rights. Importantly, a certain level of equivalence with EU regulation will need to be maintained post-Brexit to maintain access to the single market. The desire to de-regulate or change regulation must be balanced with this overarching principle.

Whichever direction regulation goes post-Brexit, brands must ensure that their approach to new regulations is in tune with the views of consumers so that trust can be maintained and built. This means taking a balanced approach to new regulations.

Foreign investment

Despite uncertainty over the future course of post-Brexit Britain, foreign companies, encouraged by weakness of sterling, may consider UK brands as targets for acquisition or investment. This could give UK brands increased opportunities for new inward investment and access to new markets. However, foreign takeovers can cause concerns for employees, customers and suppliers and have implications for brand reputation and value, requiring proactive engagement with stakeholders especially around job security and preservation of brand heritage.

Conclusions – Proactive and articulate engagement with trade bodies, the government, consumers and the media

Brexit means uncertainty, opportunities and risk. Brands, as bellwethers for consumer sentiment, need to pay particular attention to how they deal with uncertainty and risk and how they take advantage of opportunities.

Scenario and contingency planning must be at the top of management's and the board's agenda. It is important for businesses to have more than just a "Plan A". It is possible that after two or more years of negotiation, the UK could reach a constructive and positive accommodation with the EU and, quickly, with important third countries, that would allow most businesses to continue with minimal disruption. However, it is also possible that after two or more years of negotiation the UK is not in such a position and access to the EU single market and third nations could be severely disrupted with the inevitable knock-on effects for British brands.

Scenario and contingency planning should allow brand owners, ideally working as part of a sector or industry group, to engage proactively with the UK government and articulate both
their concerns relating to Brexit and areas where there are opportunities, such as in trade with third countries or in "resetting" the regulatory landscape within a sector once the UK has left the EU. Brand owners should seek to drive the discussion on Brexit planning rather than being passive and "waiting for the jelly to set".

The Prime Minister in her Mansion House speech in November 2016 called on British businesses not only to do business but to do that business in the right way, evoking the principle that business is not just there to benefit business itself but to advance the common good. This plays to the strength of the brand model and suggests brands have an important role in achieving this political vision.

Alongside uncertainty and risk, Brexit has great potential for brand owners to take Brexit opportunities, align themselves with evolving consumer sentiment and focus on the consistency and reassurance they deliver. Reputational management and effective communication will never be more important in the uncertain times ahead and those with strong UK story to tell should be particularly well-placed. Brexit will produce winners as well as losers.