



THE IMPACT OF THE KILOMETRE CHARGE ON THE LOGISTICS COSTS WITHIN THE FMCG AND RETAIL SECTORS IN BELGIUM.



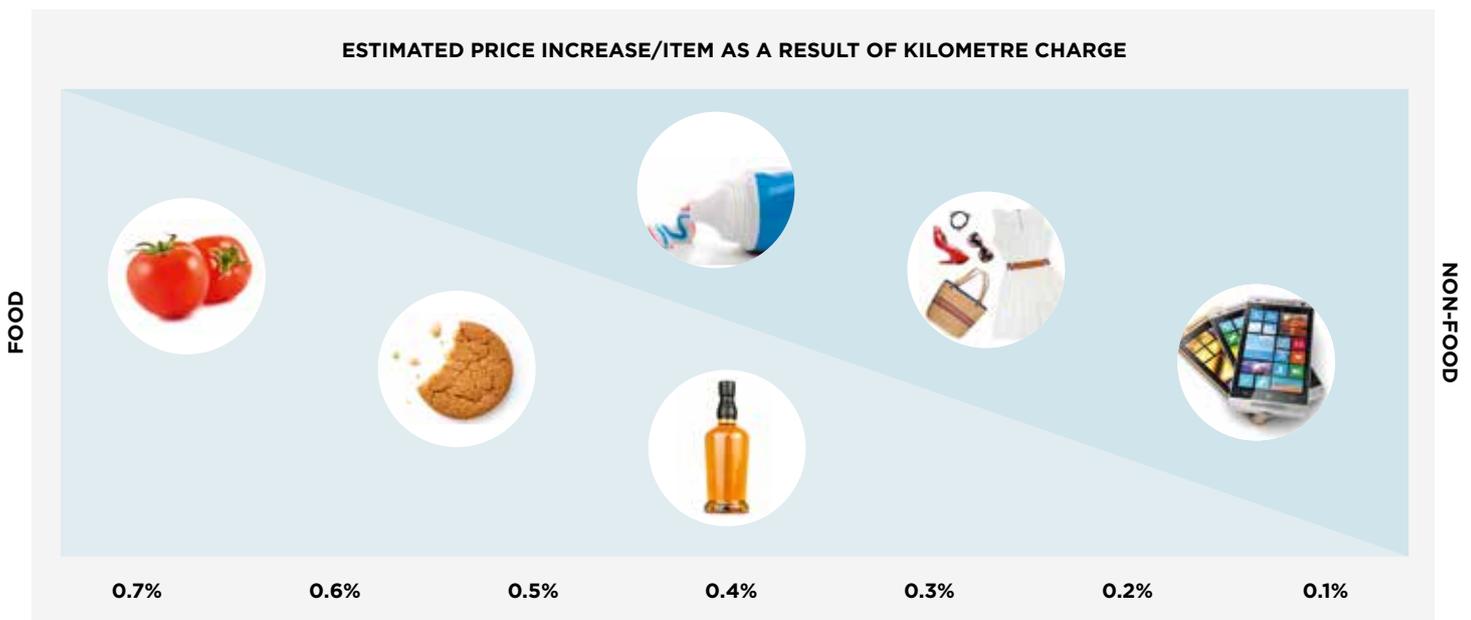
1 WHY WAS THE CHARGE INTRODUCED?

In order to reduce the number of kilometre-long traffic jams, to lower the impact of pollution on the environment, to allow foreigners to contribute more in accordance with the principle of ‘the user pays’, etc. – all responsible and worthwhile aims (MORA Mobiliteitsraad, 2010). Or rather, is the charge a new form of taxation which the consumer will ultimately bear the brunt of? Will the sector absorb this additional cost and is this actually a realistic expectation? In cooperation with PwC, The Retail Academy has investigated what is happening in the consumer goods sector and has set out the potential impact on the complete value chain. In this way, we want to provide a clear insight into what impact this measure has on the price that consumers pay for their favourite products on the shelf.

On 1 April 2016, a kilometre charge came into effect for every truck weighing more than 3.5 tonnes. Drivers can register their number plate using an ‘on board unit’ or OBU. This device must be switched on at all times when driving on Belgian roads. The price per kilometre depends on the type of road, the maximum authorised mass (MAM) and the emission standard (Euro 0 - Euro 6). The price per kilometre will also vary between 7.4 and 29.2 euro cents for each region. Those who do not have an OBU but should have one, risk a €1000 fine (Viapass, 2016).

According to the preliminary figures from Viapass, the kilometre charge generates between €2.4 and €2.6 million per day. On average, 25 million kilometres are declared every working day by 130,000 trucks on our roads. The cost of the kilometre charge therefore corresponds to an average of €18.46 per truck, per day (Belga, 2016). This could result in an estimated annual income of €720 million, however it is still too early to extrapolate these figures. Of course, a handful of compensation measures must be accounted for in the final net result. The Eurovignette has been abolished and road tax only applies to vehicles of 12 tonnes or more, which did not use to be the case (Viapass, 2016).

Is this a good thing for the state? Or are we forgetting something? Undoubtedly, there is more to say about this charge. The transport and retail sectors have many questions and doubts: what are the compensation measures, when will they be implemented, what is the long-term logistics policy of the government and how can we absorb these additional costs? Ideally, a suitable answer to these questions will emerge over the next few months.



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Of course, you can ask yourself how advisable it is to have countries apply these types of kilometre charges on an individual basis within a single EU.
Regnier Schouwenburg,
Supply Chain Manager
at Diageo (alcoholic beverages)

The Brussels-Capital Region *The Flemish Region* *The Walloon Region*

The OBU has since become a missed opportunity for a European plan on logistics transport. Even worse, European truck drivers now have to trawl through 3 extra invoices every fortnight.

A MISSED OPPORTUNITY

As the maps above clearly indicate, the strategy of the kilometre charge has since become a missed opportunity for European standardisation.

Feedback from the sector also indicates that the invoice system is complex, in view of the fact that Flanders, Brussels and Wallonia

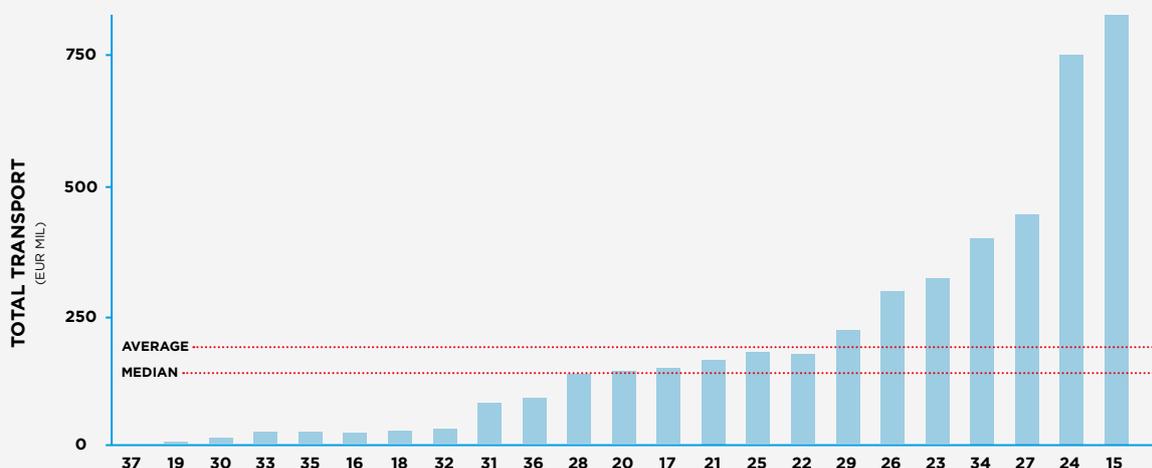
each have their own accounting system. Invoices are issued per truck and not per complete fleet. One aim is therefore to bring these together in a single invoice.

The kilometre charge in Flanders and Brussels is a tax, while in Wallonia it is a fee to which VAT is applied (Viapass, 2016).

2 WHAT IMPACT DOES THE COST HAVE ON COMPANIES OPERATING IN THE FOOD AND NON-FOOD SECTORS?

DEMAND FOR TRANSPORT BY INDUSTRY

(IN EUR MILLION, 2005)



Note: the bar charts represent the NACE (Rev. 1.1) sectors for: 15 food and beverages; 16 tobacco; 17 textiles; 18 clothing; 19 leather; 20 wood, excl. furniture; 21 paper and paper goods; 22 printing and recorded media; 23 carbon and petroleum products; 24 chemicals, incl. pharmacy; 25 rubber and plastic; 26 non-metallic mineral products; 27 basic metals; 28 metal products excl. machines, 29 machines, devices and tools; 30 office medical equipment, precision and optical instruments; 34 cars, trailers and semi-trailers; 35 other transport equipment; 36 furniture, other manufacturing; 37 recycling (Eurostat 2002b.)

Source: The importance of transport for Belgian industry and the implications of a kilometre charge on trucks (Reynaerts & Baert, 2015).

PRODUCTS WITH LOW VALUE PER M³ WILL BE HIT MOST

An investigation carried out by the University of Leuven in 2015 clearly showed the significant impact of transport on food. Food and beverages (number 15), alongside chemicals (including pharmacy - number 24), have by far the greatest demand for transport (Reynaerts & Baert, 2015).

This was confirmed by interviews with experts in supply chain and logistics in the food retail and non-food retail sectors in Belgium, which The Retail Academy held between 1 April and 20 May 2016.

The feedback confirms that products with low value per cubic metre like food would bear the greatest additional cost (Brutsaert, 2015). That is why this study mainly focuses on the food (all aspects of fresh and dry food) and near-food (this includes toiletries, beauty products and household products) chain.

In the following section, we will discuss the complete supply chain of a fresh product – the tomato – which remains Belgium’s favourite vegetable (Gfk-Vlam, 2016).

3

THE STRUCTURE OF THE COMPLETE LOGISTICS COST AND THE IMPACT OF THE KILOMETRE CHARGE

The analysis focuses on the complete value chain of a Belgian tomato. The researchers are aware that this presentation is a simplification of the reality.



3.1

FROM BASIC PRODUCTS TO PRODUCTION SITE(S) OF SEMI-FINISHED PRODUCTS

The movement of the goods (seeds, pesticides, etc.) from the farmer to the field is the start of the production chain. The impact of the kilometre charge on this type of transport is minor or non-existent, since the law does not currently include agricultural vehicles. This minor impact must also be justified on imports, since sea and air travel is often relied on. The cost of the kilometre charge on trucks has almost no impact in this respect. Depending on the product and the further production steps that must be undertaken, different semi-finished products will come onto the market. For the sake of completeness, we wish to state that the impact of the kilometre charge in the event that this tomato is processed into tomato purée, ketchup, tomato juice, etc. would be different each time.

The impact on this part of the chain is severely restricted or non-existent for packaged food, near-food and non-FMCG products as well. The first step in the production of non-food categories, such as clothes and electronic goods, mainly occurs abroad for products that are sold in Belgium.

The experts estimate a maximum increase of 3% on fresh food in this part of the supply chain.



3.2

FROM THE PRODUCTION SITE OF SEMI-FINISHED PRODUCTS TO THE FACTORY OF THE FINISHED END PRODUCT



Once the tomato travels to the factory for packing after harvesting, the impact of the kilometre charge remains low. Trucks can still be loaded efficiently. When production sites are set up, good access routes are taken into account and can ideally be accessed by rail traffic or shipping. Others opt to build the factory as close to the source as possible. Experts estimate an average increase of 1 to 3% in fresh food.

3.3

FROM THE FACTORY OF THE FINISHED END PRODUCT TO THE RETAILER'S DISTRIBUTION CENTRE



The new market share study (The Retail Academy, May 2016) highlights that the Colruyt, Delhaize and Carrefour Groups have a combined market share of approximately 70% within the food and near-food sectors.¹ However, these 3 groups combined have about ten logistics distribution centres. Transportation from the factory to a distribution centre may have a high fill rate, but the fill rate is obviously lower than transport in bulk. In addition, this step is carried out exclusively by road whereas shipping, air and rail transport were possibilities in step 1 and 2. For this type of transport cost, an increase of 3 to 5% for fresh food is realistic.

¹ The definition of the market by The Retail Academy is that 1) the retailer must generate a minimum turnover of €100 million per year (which excludes Leaderprice, for example). 2) The retailer's range must include at least some food (which excludes Di, for example). 3) The retailer must have at least 1 physical shop in Belgium. 4) Special retailers have been excluded.



3.4

FROM THE RETAILER'S DISTRIBUTION CENTRE TO THE POS (POINT OF SALE)



As a general rule, the kilometre charge will be most strongly felt by the central distribution centre of a retailer to the different shops. This presents a huge obstacle for retailers. How can they pass on the additional cost to the shops in an honest way? Can you allow an independent retailer that is located farther away from the distribution centre to contribute more than others? The feedback from the sector currently indicates that the increased prices have not yet been passed on. Different players are looking for a fair allocation solution. The retail sector itself, operating in fresh food, estimates an increase in logistics costs of between 3% and 8%.

In terms of food retail, transport accounts for approximately 50% of the logistics cost. The logistics cost is 12 to 15% of the total cost. If sell-in prices will raise by 0,3% to 1,2% (see further), retailers probably have to charge this additional cost in the consumption price. It is difficult for the food retail sector to incorporate, as it only has a net margin of 2% in Belgium.

For the non-food retail sector, the ratios are different. In this case, transport costs amount to approximately 20% of the logistics costs and the logistics cost in turn amounts to approximately 10% of the total cost. The net margins are somewhat higher in this respect.



4

WHO WILL BEAR THE GREATEST ADDITIONAL COST: THE HAULIER, THE PRODUCER, THE RETAILER OR THE CONSUMER?

Research by Graydon indicates that only half of hauliers expect to be able to pass on 80-100% of the costs of a journey. In terms of the overhead costs that this implementation incurs and the journey without loading, only 1 in 5 expect financial support from the client (Van den Broele & Verkinderen, 2016). However, hauliers are protected by two regulations on unauthorised prices² and abuse of a dominant position³. Whether these can effectively protect the transport sector remains to be seen. One great threat is the pre-invoicing of the kilometre charge for hauliers. Cashflow may become a problem for many (small) logistics companies (Graydon, 2016).



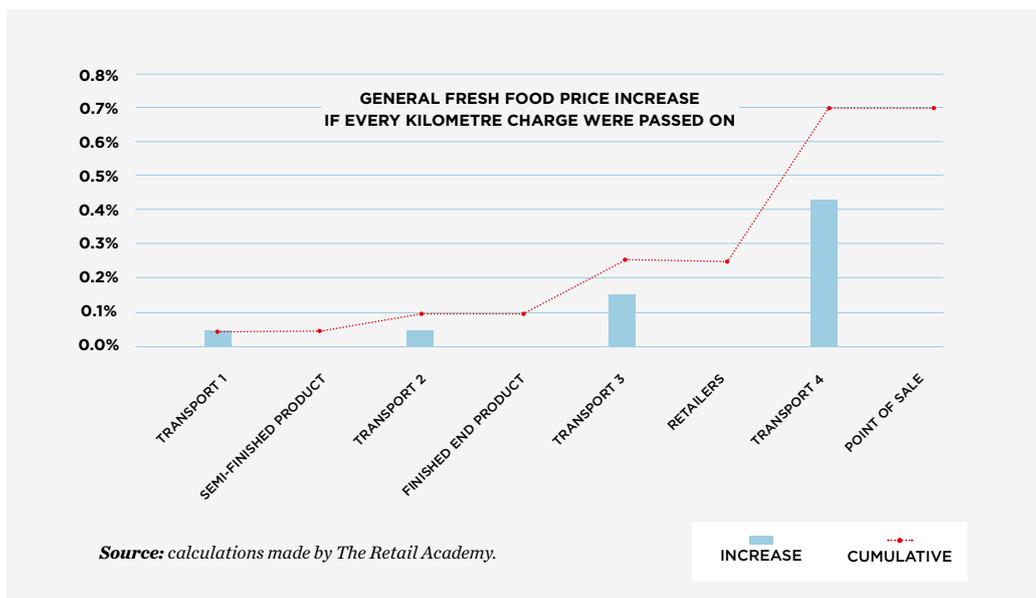
An increase of 0.7% in fresh food roughly corresponds to €15 /year. This is not a significant amount, but it is still the equivalent of an average shopping trip to a small local shop⁴.

Silvie Vanhout, Managing Partner, The Retail Academy

² The Law of 15 July 2013 on the transport of goods by road contains a number of penalties and Article 41(4) stipulates that: the haulier, the client, the freight forwarder or the forwarding agent will be fined between €500 and €50,000, with surcharges, if they have offered, carried out or arranged to carry out transport at an unauthorised low price. "Unauthorised low price" is understood to mean a price that is insufficient to also cover: - the unavoidable items of the cost price of the vehicle, in particular the depreciation or the rental, the tyres, the fuel and the maintenance; - the costs arising from statutory or regulatory requirements, particularly social, fiscal, insurance and safety costs; - the costs arising from the administration and management of the company

³ The abuse of a dominant position is based on the unilateral behaviour of one or more companies and is prohibited by Article IV.2 of the Code of Economic Law. The abuse of a dominant position can take different common forms such as: - imposing a purchase price, sales price or other unfair contractual terms and conditions; - applying excessively high prices or exclusion by the dominant company; - limiting the production quota, sales or technical development; - discrimination between trading partners; - cross-selling; - etc. As far as abuse of a dominant position is concerned, no exception may apply as an absolute ban is in place.

⁴ This calculation has been based on GfK market research figures. An average Belgian family spends roughly €5200 a year on food, 41% of which is spent on fresh food.



If the full cost is also charged at 100%, the estimated price increase for fresh products is between 0.3% and 1.1%. In the previous graph, the increase is always the average, which we used to ultimately calculate a price increase of 0.7% for fresh food.

Transport 3 will therefore feel the initial, large impact of the kilometre charge. There is a significant difference if the manufacturers in Belgium produce or not, or whether it relates to fresh products or not.

If produced in Belgium, there is more transport involved within Belgium and therefore a greater additional cost. For dry food and non-food, the need for transport is less important than fresh food, since fresh food must be delivered more frequently.

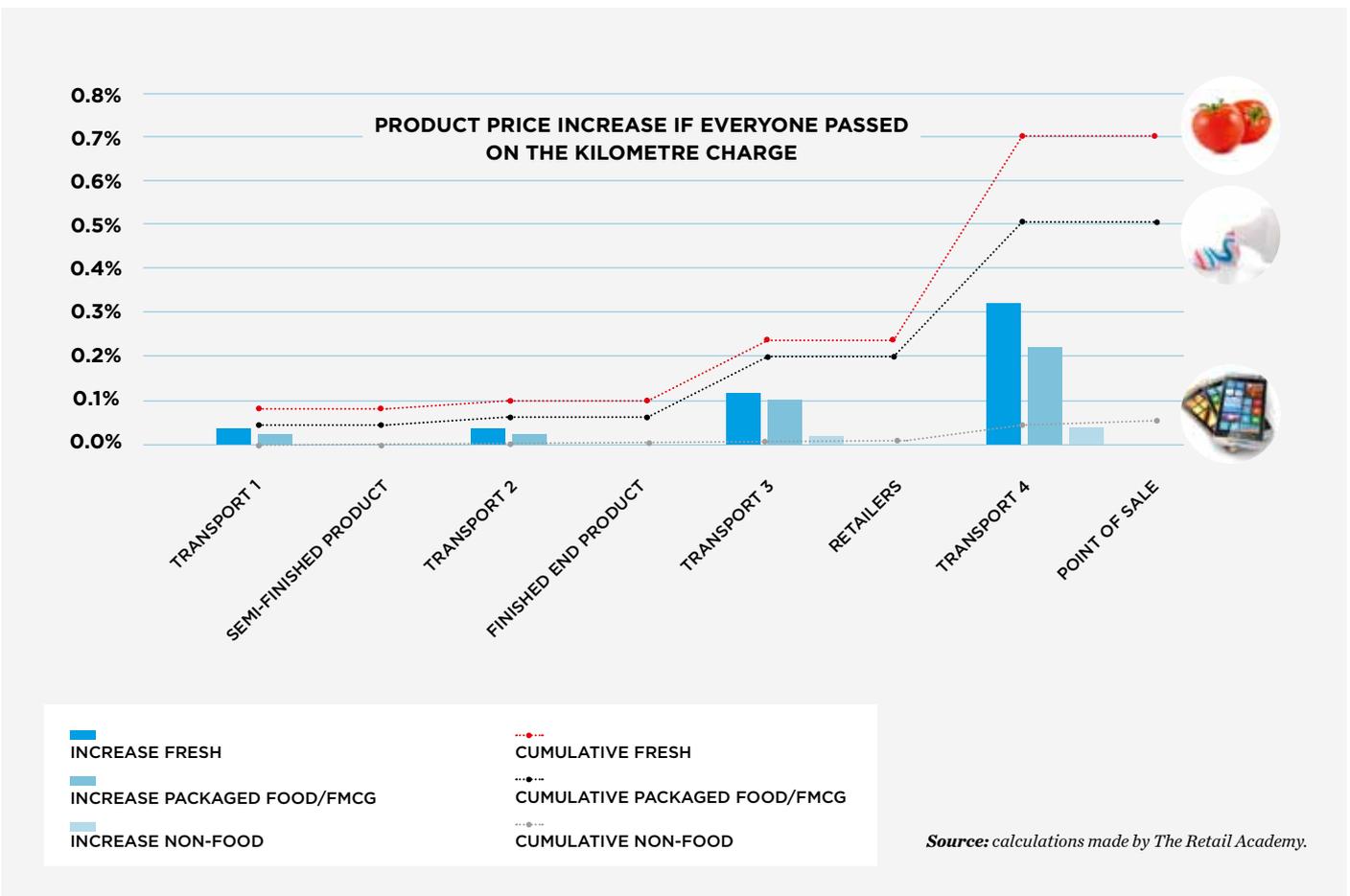
“The impact of the kilometre charge is actually a substantial cost for us. Taking detours or adapting our route is not really an option. Perhaps we will have to pass on this extra cost.”

Dirk Otto, JAVA representative for logistics and traffic, (food service)

Producers, retailers and hauliers do not have a problem with the charge in principle, if it can cohesively help to solve mobility and sustainability

issues. Rather, the question is why it has to be such a complicated system. There are countless examples abroad that are much simpler. You simply pay for the kilometres driven. The type of road or emission standards are not taken into account. The discussions also highlighted that the retail sector wants to contribute to better mobility. At the moment, the majority of people view the kilometre charge as a flat tax. Retailers are constantly trying to reduce their logistics costs. The best routes to supply the points of sale are calculated on a daily basis and they adapt their fleet to quieter trucks so that deliveries can be made overnight. The fill rates of trucks are being increased, not only for deliveries to shops, but also the return route is being looked at to utilise the capacity of trucks (backhauling) as best as possible. A small shift can be seen in smaller hauliers. There are already a number of hauliers that are adapting to smaller trucks and also looking at whether routes can be optimised without using toll roads. It is, however, too early to generalise this, since there are also hauliers that have not currently implemented any fundamental change.

The non-food sector can also expect an impact on its cost structure, but this will be much smaller. The chart below shows the expected impact on food and non-food.



Source: calculations made by The Retail Academy.



“Relatively speaking, the kilometre charge has only a small influence on our cost structure. It is exchange rates which have a greater impact.”

Ronald Boeckx, CEO e5 mode (fashion)

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“The tax must be based on the general importance to society. The idea of allowing the user to pay is not illogical. The challenge is to incorporate this measure using sustainable objectives, and to ensure that these are not too heavily balanced against specific players within our economic landscape.”

Jean-François Dohogne, Director of Product, Pricing & Innovation, Domestic Parcels, at bpost (parcels and logistics)

“Hauliers have become tax collectors for the Belgian state. The charge that we ask our clients for must be forwarded to Viapass. The increase will incur an additional cost of approximately 4% of our total turnover.”

Leo Salaerts, CEO Distrilog Group (transport)



“Truck parks are the new gold! The kilometres until the first stop are the most expensive, so by using truck parks close to the distribution centre, many unnecessary costs can be avoided.”

Jan Pijls, Director of External Logistics & Transport at Delhaize. (food retail)

5 WHAT SOLUTIONS ARE THERE?



A variety of tests are being carried out to optimise logistics, including using eco-combi vehicles, route optimisation, backhauling, training the driver to adopt environmental ways of driving, optimising the fill rate, etc. Fevia is advocating allowing the transportation of 36 pallets instead of the current 33 pallets (De Bock, 2016). More and more interesting initiatives are gradually resulting in more efficient logistics.

But are these measures enough? Do retailers have to consider decentralisation or other measures in the long term?

And how are producers going to respond? Are they going to work together creatively to share and reduce the logistics costs?

Only time will tell.

QUESTIONS FOR FURTHER RESEARCH

In this white paper, the greatest difference uncovered was between food and non-food. It would be fairer to carry out an analysis per consumer good and the location of production. Goods that have been produced abroad and supplied to Belgium are ultimately less affected by the increased cost as a result of the kilometre charge. This would make this study needlessly complex, but is an interesting analysis that each company can interpret for themselves.

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