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How tariffs could be a blessing in disguise for American companies

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Jerry Haar

All indications are that free trade has gone the way of the typewriter and the pay phone. What has long been a pillar of economic liberty and free-market capitalism has been degraded by protectionism, populism and isolationism. Neo-mercantilism is the flavor of the month.

Despite the fact that, over the past 20 years, nearly 90 percent of economists have supported eliminating tariffs and two-thirds of Americans believe tariffs will lead to higher prices, tariff increases are here to stay. Exporters, importers, producers and consumers will all be negatively affected by tariffs.

But does this cloud have a silver lining? The answer is a resounding yes.

The problem with trade policy (in fact, with all economic policy) is that it is conceived, planned and implemented by economists, lawyers and bureaucrats who are far removed from the real world of commercial transactions. As such, they are very often oblivious to the impacts of trade policy on producers and consumers.

The silver lining of tariff increases is that they will force companies to assess (and reassess) their efficiency and productivity. Tariff increases will hold their feet to the fire, so to speak. An export-oriented nation with a strong currency, such as the U.K., is faced with the dual challenge of having their exporters price goods to make them affordable for importers (trimming their sales margins) while being slammed by a tariff increase. A currency devaluation is not the answer, especially if the exporter needs to source inputs/components from a strong-currency (and therefore more expensive) supplier.

In order to effectively respond to tariff increases, an import company must recognize it has four options: pass the tariff increases along to their customers, absorb the tariff (resulting in lower profits), renegotiate contracts with suppliers or switch suppliers.

The firm must conduct an internal audit of its operations to gauge efficiency, effectiveness, productivity, competitiveness and sustainability. A well-led and well-managed enterprise would want to do this anyway on a regular basis. Such a "health check-up" would include all units of a company's operations: finance and accounting, sales and marketing, human resources, production, IT and customer service.

Once the check-up is complete and the company institutes necessary improvements, what are some of the most important changes it can make with respect to tariff increases it faces?

The company must review in detail the free trade agreements the nation has in place with the trading partner to determine where the company may have advantages over competitors that are not member of a free trade agreement.

As for unfair trade practices of foreign exporters, in the case of trade with China, companies need to have a clear understanding of Section 301 of the Trade Act of 1974, which provides a statutory means by which the U.S. imposes trade sanctions on foreign countries that violate trade agreements or engage in acts that are "unjustifiable" or "unreasonable" and burden American commerce.

The poster child for unfair trade practices is, of course, China. Over the past three decades, China has dislodged manufacturing operations in countries in the Americas and eroded U.S. markets in the region.

Another important means to lessen the immediate effect of tariffs is the foreign trade zone, whereby foreign merchandise "parked" in such a zone is not hit with a tariff until it leaves the zone. (Think glass Christmas ornaments from Poland that arrive in the U.S. in August with duty paid only when they leave the zone in November.)

According to Gary Goldfarb, chief strategy officer of the third-party logistic firm Interport, "Leveraging a Foreign Trade Zone (FTZ) can help mitigate potential cost increases. Our FTZ facilities allow businesses to defer duties on imported goods until they leave the zone, avoid tariffs on re-exported items, and eliminate duties on scrapped or destroyed goods. These cost-saving measures help ensure that our customers' supply chain remains competitive despite evolving trade policies."

A somewhat related mechanism is the "duty drawback," whereby 99 percent of the duty is refunded to the importer if the product is re-exported. Still another means is "tariff engineering," whereby customs brokers or trade lawyers can find a way to lower the tariff rate by reclassifying the product. Of course, sourcing from a different locale — supply chain diversification — can not only lower the import cost but spread the risk by adding another source of product importation. Also, importing components for final assembly, rather than finished goods, to reduce or eliminate the tariff load can be cost-saving as well.

And let's not forget the role of technology. Import-export software has been a boon to international trade, as it has streamlined logistics and compliance processes. The software may be used in centralized data management, automated workflows and trade finance management. Thomson Reuters's Onesource Global Trade and Descartes Datamyne are but two of the leading firms that efficiently facilitate cross-border commerce.

The Reagan-Thatcher era is over. Tariffs and tariff increases are with us now and will be for the foreseeable future. Companies engaged in cross-border commerce need to adjust to this reality — and in so doing, they may actually find a silver lining in the cloud of neo-mercantilism.

Jerry Haar is a professor of international business at Florida International University. He is also a fellow of the Woodrow Wilson International Center for Scholars in Washington, D.C., and the Council on Competitiveness.