

Recent Tariffs and Their Impact on the Construction Industry

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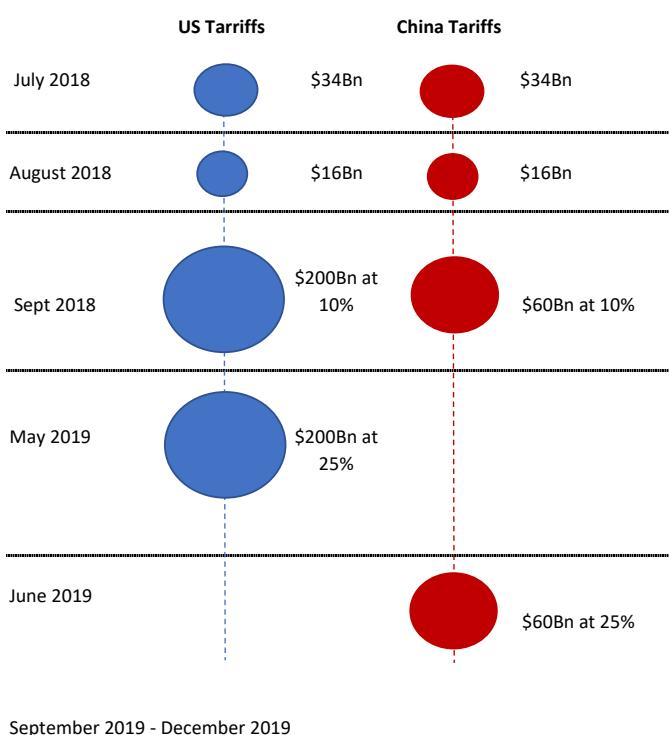
Abstract

The trade war between the U.S. and China has resulted in a series of tariffs from both countries that have had wide-spread impact on the construction industry. In this paper, Cumming Vice President and economic expert Dan Pomfrett takes a closer look at the details of these tariffs, including the rationale behind their implementation, their effects to date, and what to expect going forward.

Overview

With tariffs continuing to play a large and volatile role on construction projects, it is important to understand the details of these tariffs, as well as their potential impact on the industry as a whole.

How the US-China trade war has escalated



Source: BBC Research

How did we get here?

As we all know, the tariff saga has been a long-burning one that really started gaining traction in late 2017 and early 2018, when the U.S. Department of Commerce commenced an investigation under section 232 of the Trade Expansions Act of 1962, the purpose of which was to determine if U.S. imports of steel and aluminum threatened national security. They concluded that imports were weakening the internal economy and made tariff recommendations that focused mainly on supporting domestic buyers while remaining favorable to sellers. The ultimate goal of these tariffs was to "bring back" domestic steel and aluminum production. Over the last 12 months, four additional rounds of tariffs were introduced, affecting more than \$360 billion worth of Chinese products, and \$110 billion worth of U.S. products.

So how did this work out?

Depending on your position in the consumer line, results have ranged from good to bad. Following the tariffs, suppliers and manufacturers found themselves in a tricky position: on one hand, the tariffs allowed them to avoid external price pressure, with many already at their breaking point with production costs; but on the other hand, it meant that those obtaining lower-cost raw materials would need to take a further hit when prices rose, leading to the difficult decision of whether or not to pass these cost increases through to consumers. For many, the first round of tariffs were a welcome relief; but as the second, third, and fourth rounds came into play, the continued cost increases could not be absorbed by the manufacturers and were ultimately passed to the US consumer.

This has created a tipping point: now, rather than being perceived as an aid to the US economy, the tariffs are being seen in some quarters as increasingly detrimental to the US consumer.

Interesting arguments have been put forward by companies such as Apple, which sources manufacturing from China. Because of this, they argue that they have been negatively impacted compared to key rivals such as Samsung, which sources manufacturing from South Korea and is therefore tariff-exempt.

What has been the impact to the U.S. economy?

U.S. GDP growth is expected to continue its deacceleration from a high of 3.0% growth in 2018 to 2.3% in 2019 and 1.8% in 2020. The trade negotiations with China remain the largest unknown: new tariffs were implemented in the second quarter of 2019, the effects of which are still playing out. The consensus appears to be that this will have a detrimental effect on the economy as a whole, although there are businesses that will likely benefit from the tariffs. Fears remain of an oncoming recession in 2022/23, and many domestic companies are putting expansion plans on hold while they see how the economy shakes out over the next 12 to 24 months.

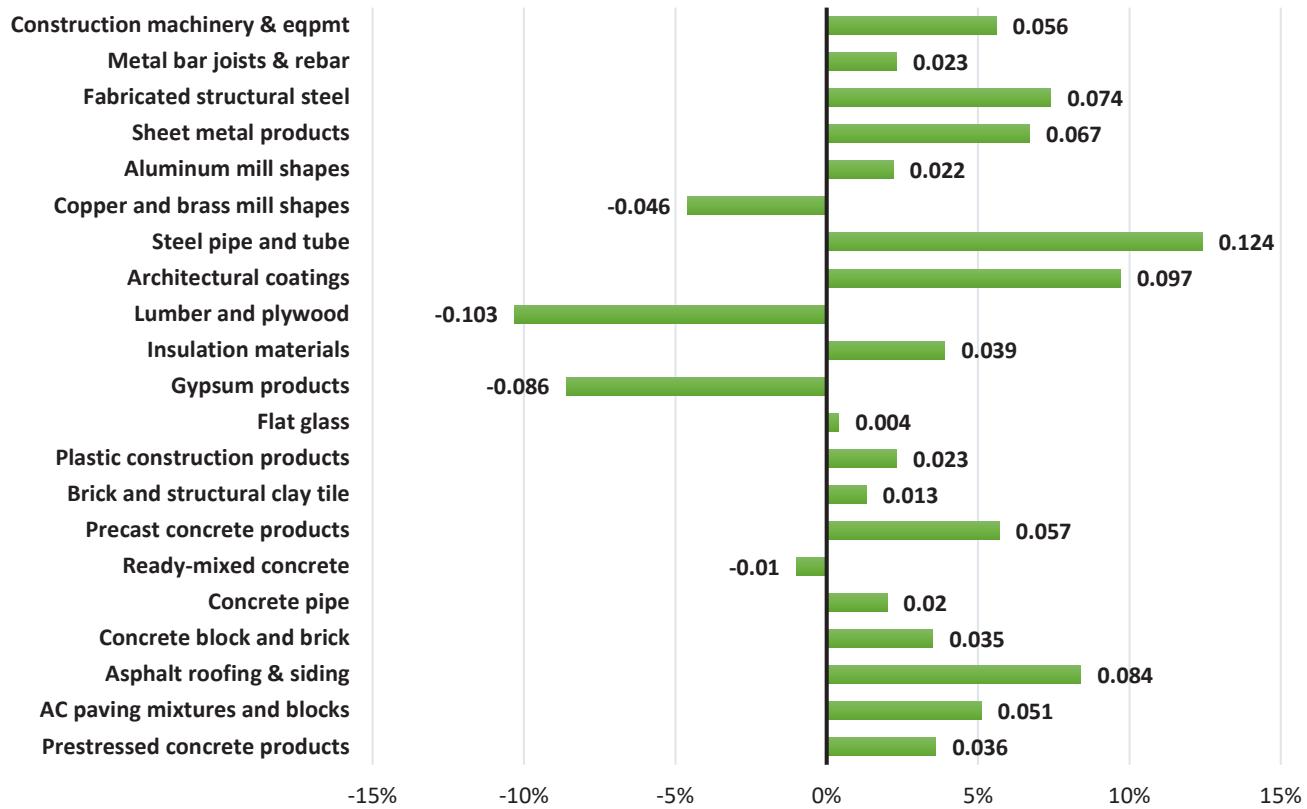
The impacts of the Chinese tariffs have yet to fully hit the market. The final list of items remains to be determined and

are in the appeal process. One interesting note about Section 301 sanctions is that the tariff is determined by the specified part's country of origin, rather than where it was assembled. For example, a backhoe or truck imported from Japan could be subject to some portion of the Section 301 tariffs if any of the parts used in that machine were made in China.

How have tariffs affected domestic material pricing trends?

This is a hard question to answer. While the tariffs have certainly had a big impact on costs, material prices have been affected by many other issues as well, including an overall market slowdown (which some are saying is indication of a future recession), natural disasters, fuel costs, and political factors.

Construction Materials Price Movement - Last 12 Months



Source:
US Bureau of Labor Statistics

Is it just China who is affected?

No. The U.S. tariffs, along with import caps, reach beyond China, with the European Union, Turkey, Russia, and India all feeling their effects. As a result, these affected regions are all applying retaliatory tariffs of their own, which range in product and percentage applied, but which may be increased further still without some sort of agreement or compromise. The value of goods to which these tariffs apply are less than the value of goods affected by the U.S. tariffs, but these actions will hurt the consumer regardless, as price increases will likely be passed on. It is also worth noting that China, the European Union, Canada, and Mexico are the United States' largest trading partners.

What happens now?

Negotiations are continuing and will likely continue to do so for some time, as both the US and China jostle for position. Estimates for the latest round of tariffs vary, but the overwhelming view is that this will add a cost to the U.S. economy. Add the European Union and others, and it is clear that the negotiations will need to be carried out on multiple fronts. It is anticipated that agreements will ultimately be reached, but the details of any such agreements remain to be seen. Questions will also be raised about the long-term trading relationship between the countries as this whole episode is likely to leave a very sour taste in the mouth for all of those involved.

US Tariffs	
Section 232	Steel 25%, Aluminum 10%
Section 301 – List 1	25% to 30%
Section 301 – List 2	25% to 30%
Section 301 – List 3	25% to 30%
Section 301 – List 4	15%

Retaliatory Actions	
Canada	10% to 25%
EU	10% to 50%
Mexico	7% to 25%
China	15% to 25%
Japan	Multiple
Turkey	5% to 40%



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Dan is a Vice President at Cumming, as well as our National Director of Forecasting and Analytics. He holds a B.S. degree in quantity surveying, is a certified member of the Royal Institute of Chartered Surveyors, and has more than 20 years of industry experience. He also researches and writes Cumming Insights, the company's quarterly report that breaks down economic trends and projections for regional construction markets across the country. In addition to his work in economics, Dan has provided cost-related services for numerous high-profile clients, including international architectural firms, museums, cultural institutions, and private developers.