Grant Thornton

Navigating tariff uncertainty: strategies to adjust and thrive

Teaser Video Transcript

Tariffs and Economic Trends

I'll do my best here in in a short amount of time. But, you know, tariffs are essentially taxes on imported goods. They look a lot like consumption taxes. And so there's strong linkage, right, between tariffs, larger economic trends and related traditional tax planning. So, Colin mentioned tariffs are generally imposed on the importer, of record. But economically, the burden of tariffs is shared, right? And it could end up with the producer, it could end up with the seller, it could end up with the customer. And I think that as we look at this issue, that's kind of the huge question that people are asking themselves now is where are those burdens of those tariffs going to fall?

How much am I going to be able to pass on in price? How much am I going to have to fix through supply chain? How much are suppliers going to have to give up, especially if they're foreign suppliers impacted heavily by those tariffs? So when you look at the broader economic trends, the first one I see is that tariffs are typically thought to be inflationary. I know this, the CBO, the Congressional Budget Office, when they look at these, they say, yes, tariffs are thought to be inflationary. So whether that comes through like direct increases in prices for customers or whether it comes through increased pricing power that domestic manufacturers might have as foreign good prices increase, you're going to see some potentially inflationary effects, right?

That creates a feedback loop. And as the Federal Reserve thinks about monetary policy, if they see inflation start to be persistently pressured upward, I think we know that the Federal Reserve becomes reticent about cutting rates in that environment. They potentially even look to raising rates to tamper down the effect of that inflation. Increased interest rates come in a particularly difficult time when you think about them in the perspective of tax. Part of the Tax Cuts and JOBS Act back in 2017 introduced significant curbs on company's ability to deduct interest expense. And those curbs have only become tighter.

And so a big part of the tax policy debate going forward is what will the deductibility of interest expense look like, which is a major issue for companies that are funded with debt because they have to understand what's that going to have an impact on from a cash flow perspective? How's it going to affect my ability to service this debt and what can I do to respond to a persistent high interest rate environment. So the second one that I wanted to talk about was kind of consumer demand, kind of an offset to some of these inflationary pressures. You know, tariffs can be a little bit regressive.

You think about them as a tax and you think about the incidents falling on the consumer, lower to middle income taxpayers that maybe have spending that's less discretionary, right, and more unstable type products, they're going to be impacted by higher prices disproportionately. So certain companies might find themselves faced with downward pressure on demand, which could impact their overall tax strategies. When you think about companies that are seeking to invest heavily in R&D and R&D is a huge topic in the tax debate right now, the recoverability of R&D costs, R&D incentives, they're proliferating around the world in complex tax mechanisms. Those companies may need to realign their thinking on R&D.