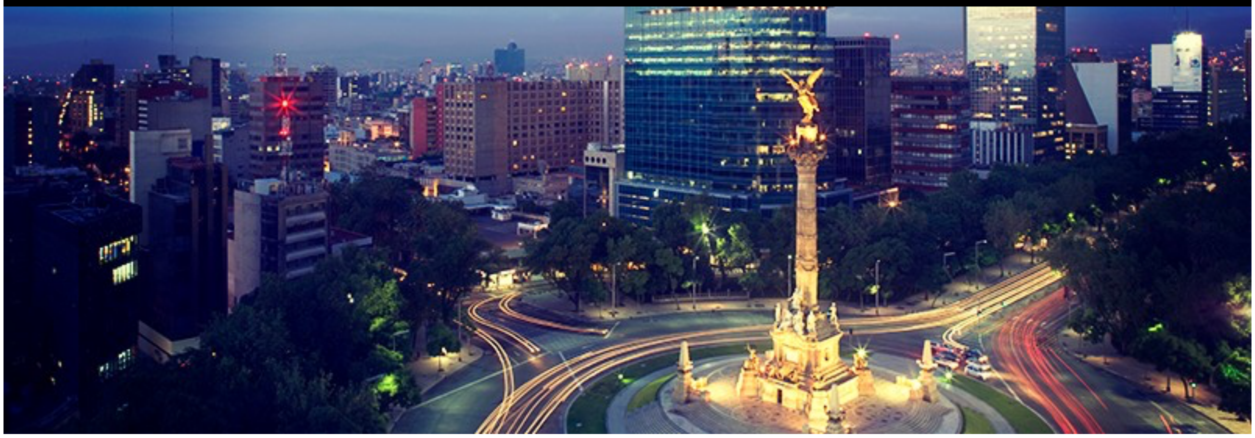

Monarch News

Navigating the Tariff Threat to North American Trade

February 5, 2025

Executive Summary

On February 3, 2025, the Trump administration announced a one-month delay in its intention to impose a 25% tariff on products imported from Mexico and Canada, two of the country's most important trading partners. While this postponement has temporarily eased tensions, the threat of tariffs remains, leaving investors on edge and businesses across North America in a state of uncertainty. Tariffs risk disrupting critical supply chains that, over many decades, have emerged to make North America the single most competitive economic platform in the world. Our three countries – Mexico, Canada and the United States – do not just trade in isolation. Rather, we work in a seamless coproduction value chain that creates jobs and sustains livelihoods across the entire continent. At a time when the United States should be locking arms with its North American partners to deepen economic cooperation to compete against Chinese and other ascendant competitors, the country appears to be on the verge of doing just the opposite. If you are scratching your head, regardless of your residency or political preferences, you are not alone.

The announced reprieve in the imposition of tariffs, and the corresponding retaliatory tariffs, is encouraging, but companies are by no means out of the woods. Trade and commerce loathe uncertainty, and companies are finding it challenging to know how to navigate key decisions related to supply chain resilience, investment decisions and workforce management. Thus, while the politicians work furiously to chart a course to a political resolution—the key benchmarks for which are *still* unknown—companies must leverage this pause to chart a course into an unknown future.

For nearly a quarter century, Monarch Global Strategies has helped our clients navigate the U.S.-Mexico trade and investment environment, from both sides of the border. In our experience, there are some basic approaches every company should be taking now to mitigate the risk of tariffs, which we summarize briefly below. Of course, any possible response varies by sector and its corresponding vulnerability to tariffs, but in our judgment these are common sense tactics every company should be evaluating.

Recommendations for Managing Tariff Impact

- Explore legal avenues to challenge or mitigate the impact of new tariffs (including looking for exceptions).
- Estimate the net impact of tariffs on products and inputs and overall profitability.
- Assess the potential need to change the company's investment strategies (in the short-term).
- Develop a clear communication plan for stakeholders. The company's stakeholders should be informed of the impacts that tariffs could have on the company's bottom line and what specific actions the management is taking to mitigate these potential effects.
- Create a specific communication plan for clients and suppliers. Careful and specific communication and consideration of options can put manufacturers (client and suppliers) on track to not only navigate their new environment but build resilience for any other changes ahead.

- Establish learning processes and performance indicators to track the actions taken, periodically recalibrating the strategy (e.g., every 3 to 6 months).
- Speak with your bankers (as soon as possible) about covenant ratios and compliance with bank agreements and request waivers if necessary.
- Assess the potential relocation of production centers to locations with lower tariff rates and more competitive production costs (particularly if the tariffs appear to be permanent and you would be non-competitive in the current location).

Recommendations for Cost Reduction

- If new tariffs apply to production inputs, evaluate how best to prevent these costs from being passed onto the company.
- Develop and implement an aggressive cost reduction strategy to partially mitigate the combined impact of tariff increases on sales and production.
- Investigate alternative sources for production inputs in countries with more favorable tariff rates.
- Develop relationships with suppliers in countries with better tariff conditions.
- Formulate contingency plans for critical inputs in the production process, given the possibility that rising supply chain costs could lead to bankruptcies of existing suppliers.

Recommendations to Mitigate Impact on Sales

- Assess the feasibility of raising prices to offset tariff increases.
- Analyze demand elasticity in response to potential price hikes.
- Evaluate the impact on profitability with a sensitivity analysis to tariff levels, price hikes, and demand fluctuations.

- Segment customers by their sensitivity to price changes.
- Investigate opportunities to export products to countries with no tariffs. Identify the necessary steps to market these products abroad.
- Prioritize the best current clients (based on the margin obtained per client).
- Consider differentiated pricing for different customer segments.
- Move final products that could be subject to tariffs to the U.S. as soon as possible.
- In case of supply shortages, analyze how inventories will be distributed based on the margin per client.

Monarch Global Strategies certainly hopes that a trade war between Mexico and the U.S. can be avoided through dialogue and cooperation, fostering a more balanced and reciprocal trade environment that benefits industries across North America. Still, it is best to be prepared for any situation.

If your company operates in sectors such as automotives, medical devices, aerospace, electronics, or energy—industries that could be impacted by these trade developments—please contact us. We have a strategic approach designed to support you in navigating these uncertain times.

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