

# AS TARIFFS EXACERBATE HEADWINDS FOR OIL & GAS, GO LEAN AND DIGITAL

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**Trade tensions and tariffs have exacerbated negative headwinds facing energy companies in an already chaotic global market. The current climate requires a forward-thinking strategy to navigate current turbulence and adapt for long-term success.**

Amid U.S.-China trade tensions, companies must calculate the immediate impact of tariffs and plan for what a continued trade war with China will mean for their businesses. These concerns compound the existing challenges of operating in a low oil price environment and investor pressure to focus on profitability, which translates to decreased availability of new capital.

Facing multiple negative pressures, oil and gas companies need to lower costs and improve efficiencies if they are to survive and thrive.

## A RECAP OF TRADE TENSIONS' IMPACT ON OIL AND GAS

Oil and gas companies have been adversely impacted by China's 25% tariff on liquid natural gas (LNG), which went into effect on September 1, as well existing U.S. tariffs of 25% on Chinese steel.

Since the tariffs were implemented, predictably, Chinese imports of U.S. LNG have fallen and imported steel prices have increased. Unless the trade war abates, Chinese imports of U.S. LNG will likely continue to remain at lower levels or decrease further, which means U.S. exporters will need to find other markets for

their product. Increased steel prices mean higher costs to build much-needed new pipelines, which could erode profit margins even further.

If the trade war continues, natural resources companies could have another huge issue to contend with, namely: China raising the prices of rare earth materials. This could harm numerous sectors, including renewables and energy storage. Tensions between China and Japan in 2010 caused a pronounced rise in the price of rare earth materials, and new fears of a potential embargo already caused a spike in those prices as of May 2019.

Tariffs are just one of several factors impacting oil and gas companies, however, and a new trade deal with China will not relieve all the pressure on the industry. Low oil prices—which may see a short-term boost following the drone attacks on Saudi Arabia's production facilities—and reluctance to provide new capital will continue to threaten survival.

To overcome these conditions and have continued success in the future, oil and gas companies must follow two strategies: Go lean and go digital.

## GOING LEAN

Going lean means improving operational efficiency—cutting costs and streamlining processes to improve organizational health. This may necessitate consolidation, divestitures, restructuring and even management changes. Going lean may also require

that companies reexamine their supply chains—especially if they have significant ties to China—and adjust their sourcing to reduce exposure to tariffs. They may also need to reexamine their pricing structures if their capital input costs have increased and they need to pass those increases to their customers.

When assessing tariff exposure, companies should engage customs professionals with deep expertise in this very technical area to determine total tariff liability—or a company's entire exposure to tariffs throughout the supply chain. There are several strategies for legally lowering the duty value owed. For example, companies may be eligible for a refund if they've been applying incorrect tariff codes to their products. Determining whether merchandise has been properly classified under the Harmonized Commodity Description & Coding System (HS) is as much an engineering exercise as a legal one—companies need to evaluate the nitty-gritty details of, for example, product measurements, material composition, and how the product is used to determine its correct tariff classification. While this can be a tedious process, digging into the details of every single product is one of the most effective ways to minimize your tariff liability.

## GOING DIGITAL

Going digital means investing in technologies to drive operational excellence while boosting profit margins, improving safety and reducing speculative risk. These new emerging technologies—blockchain, artificial intelligence and machine learning, cloud computing and internet of things (IoT)—have increased potential within natural resources to meet these goals, and in many cases within existing systems.

In the exploration sector, seismic imaging presents one example of how technology can create value. While seismic imaging already

involves analytics and 3-D visualization models, some exploration and production companies have been able to construct 4-D models using data analytics, map changes in the levels of oil and gas reserves and even predict the lifespan of wells. A greater degree of real-time data to drive trends, patterns and insights enables companies to make more informed decisions earlier in the process, thus greatly reducing the cost of exploration investments while increasing the probability of extraction success.

## BALANCING IMMEDIATE NEEDS AND LONG-TERM SURVIVAL

Natural resources companies face a tough balancing act: pursuing digital transformation and operational efficiency while minimizing expenditures, navigating trade and tariff disruptions, low oil prices and investor pressure. But it's an imperative that they can't afford to ignore—companies that don't invest in their future risk falling behind those that do, and one day may find themselves unable to catch up.

To learn more about strategizing around tariffs and customs issues, as well as how natural resources companies can get started developing and deploying a digital transformation strategy, take a look at the below Insights:

- ▶ [Achieving Operational Efficiency Through Digital Transformation](#)
- ▶ [10-Percent \[Now 15%\] List 4 Tariffs to Begin September 1](#)
- ▶ [Top 10 Considerations for Customs Planning in 2019 and Beyond](#)
- ▶ [Analytics & Insight](#)
- ▶ [BDO & Pitchbook: Natural Resources M&A Report](#)
- ▶ [Section 301 Tariffs](#)

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