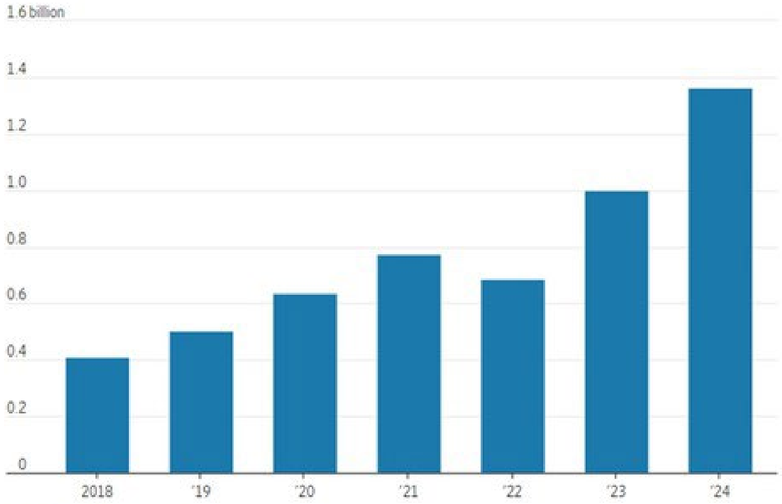
Tariffs, the De Minimis Exemption / Temu & Shein Impact

The de minimis exemption (DM), originally created for duty-free entry of low-value goods, inadvertently became a powerful competitive edge for e-commerce giants like Shein and Temu, placing traditional U.S. retailers at a distinct price disadvantage.

- Established under section 321 of the Tariff Act of 1930, the DM allows for goods under $200 to enter the U.S. duty-free. In 2015, the duty-free limit was raised from $200 to $800 per person daily.
- Shein and Temu capitalized on the rule change by breaking bulk shipments into small parcels, avoiding import duties and gaining a pricing advantage over U.S. retailers, who pay duties on bulk imports. The strategy has been successful, with shipments under the DM skyrocketing. In 2024, 1.36 billion shipments entered the U.S. under the DM provision, up 113% from 637 million in 2020, with Shein and Temu accounting for more than 30% of the shipments.
- With the boom in shipments, sales for Temu (owned by PP Holdings, Inc.) and Shein have soared, as consumers attempt to stretch their budgets with cheaper alternatives (see below).



Note: Fiscal years ending Sept. 30
Source: U.S. Customs and Border Protection

*2022-2023 revenue data from Daxue Consulting, Forbes, FT

On February 4, 2025, executive orders went into effect that:

- Prohibited DM treatment for Chinese shipments valued at $800 or less. However, the order has been temporarily paused since February 7 to allow the government and businesses time to reengineer their systems to monitor, report and collect the additional import duties.
- Increased tariffs on most imports, notably 25% for select Canadian and Mexican goods and 20% on Chinese products, effective March 4, 2025. For context, in 2024, average U.S. apparel tariffs ranged between 12% and 17%, costs that domestic retailers had to absorb or pass on to consumers.
- Triggered retaliatory tariffs from China, Canada and Mexico. China implemented 10% to 15% tariffs on select U.S. imports, including agricultural products, semiconductors and automobiles. Tariff negotiations with Canada and Mexico are ongoing.

Revoking the DM threshold on all foreign goods could provide much-needed relief for U.S. retailers, notably smaller specialty chains facing e-commerce competitors offering greater variety at lower costs. There are calls from U.S. industry groups (e.g., National Council of Textile Organizations, the Alliance for American Manufacturing and the American Federation of Labor and Congress of Industrial Organizations) to end the DM on all commercial shipments from all countries to prevent a shifting of the source country.

There are also claims that the DM is being manipulated to import counterfeit apparel and pharmaceuticals, hazardous infant products and toys, imitation automotive components and goods produced through forced labor that are shipped directly to consumers, which the government is addressing through greater disclosure requirements.

Apart from the DM, Shein and Temu's rise mirrors the challenges of past retail giants such as Sears, J.C. Penney and Express inc., who failed to adapt to the changing market dynamics brought on by Amazon. Among the brick-and-mortar retailers currently feeling the strain are fast fashion chains (e.g Forever 21) as well as Cato Fashions, Citi Trends, Carter's and Tilly's. Notably, even Amazon's 2024 attempt to launch a Temu copycat, "Haul," is not gaining traction with consumers, and U.S. brands using Shopify are battling against direct-from-China sellers' pricing advantages.

The adjacent chart shows the operating performance of Temu's parent PDD Holdings, Inc.

PDD Holdings, Inc. (in billions) Yuan 6.38 = 1US$	3Q24 9/30/2024	TTM 9/30/2024	FYE 12/31/2023	% change TTM24/ FYE23	USD FYE23
Revenue	¥99.5	¥372.1	¥247.6	50.3%	$38.9
Operating Profit	¥24.3	¥105.2	¥58.7	79.2%	$8.3
Operating Margin %	24%	28%	24%	19.3%	21%
Free Cash Flow	¥27.5	¥128.7	¥93.6	37.5%	$14.7
Cash	¥125.7	-	¥121.8		$17.1
Total Debt	¥10.2	-	¥10.2		$1.6

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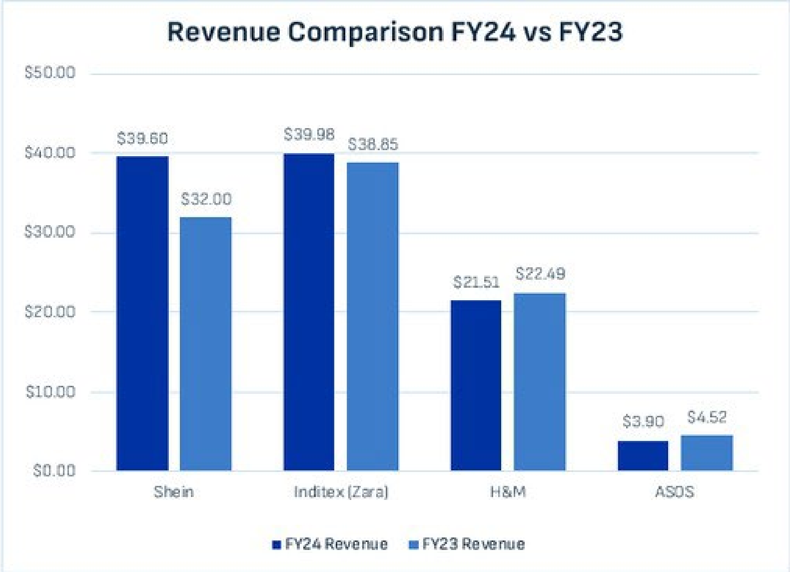
Impact on Fast Fashion: H&M, Zara, ASOS



Exchange Rates Used:
USD to SEK on 11/30/23: 1 USD = 10.496 SEK
USD to EUR on 1/31/24: 1 USD = 0.9251 EUR
GBP to USD on 9/3/23: 1 GBP = 1.2781 USD
USD to EUR on 1/31/25: 1 USD = 0.9662 EUR
GBP to USD on 9/1/24: 1 GBP = 1.3434 USD

Shein and Temu started noticeably disrupting the retail industry around 2020 by:

- Offering trending products at ultra-low prices
- Capitalizing quickly on fashion trends via TikTok and Instagram
- Driving up advertising and customer acquisition costs for other retailers

Even established European fast fashion leaders under our coverage, H&M, Zara, and ASOS, have had to recalibrate their businesses to respond to the competitive threat as follows.

- H&M has struggled to maintain price competitiveness while keeping to stricter sustainability and regulatory standards. The retailer has responded by reducing excess inventory, focusing on higher-margin items, and experimenting with resale platforms, and sustainability-focused collections.
- Zara has adjusted by further shortening its supply chain. Unlike Shein, which relies on thousands of contract manufacturers in China, Zara has regional production hubs (e.g., Spain, Portugal, and Morroco) that allow rapid restocking without relying on long shipping times.
- ASOS, once an affordable fashion icon, is losing market share to Shein. ASOS has implemented a "Test and React" strategy, allowing it to react faster to changing trends, shifting its marketing strategy away from heavy discounts, investing in its proprietary brand, and focusing on bestsellers.

Summary and Outlook

While eliminating the DM exemption and raising tariffs aim to create a level playing field for U.S. retailers, Shein and Temu's success is not solely dependent on the loophole's price advantages. Their digital-first, trend-focused and efficient business models are key. The trade landscape remains volatile, with tensions between the U.S., China, Canada and Mexico escalating, disrupting global supply chains. Meanwhile, Temu and Shein are not standing still; they have expanded their U.S.-based operations. Last year, Temu began onboarding Chinese sellers with inventory in U.S. warehouses, enabling faster shipping within the U.S. and Shein opened distribution centers in Illinois and California in 2022 and established a supply chain hub in Seattle last year. According to published reports, Shein recently confirmed its intention to float on London Stock Exchange.