

Intelligence MEMOS



From: Daniel Schwanen
To: Trade Observers
Date: January 16, 2025
Re: **MR. TRUMP'S RUINOUS TRADE WAR (PART ONE)**

Incoming US President Donald Trump has threatened to impose 25-percent tariffs on goods Americans purchase from Canada. The impact of this measure on trade between Canada and the United States will not reduce the US trade deficit with Canada, one of the measure's stated goals. Instead, it will damage both the Canadian and American economies.

Canada's objectives should be initially to reduce the damage, increase its leverage in any negotiation, and eventually address key US concerns sufficiently to get the tariffs removed.

Mr. Trump initially suggested that the tariffs would only stay in place until Canada addressed illegal immigration and drugs crossing into the United States. But the chances they will lift once these issues are addressed – an assessment solely in US hands – are extremely low, even though Canadians are perfectly willing to address these concerns. Mr. Trump is likely to want the tariff to remain for economic reasons, including raising revenues to cover the gaping US fiscal hole, and eliminate the US trade deficit with Canada.

Mr. Trump considers this deficit a US "subsidy" to Canada, even though it is the result of myriad transactions willingly entered into by buyers and sellers on both sides of the border.

Yet this deficit is entirely accounted for by US purchases of oil and gas, and other industrial materials (See Figure). These directly support US competitiveness. Exhibit A in this respect are US imports of oil and gas from Canada, which allows the United States to generate its global trade surplus in petroleum products while keeping energy prices down for Americans. Certainly, if it wanted to reduce its trade deficit with Canada, the United States could boost its own oil and gas production (as it intends to do), or switch to other, more expensive, sources of oil.

Meanwhile, the United States registers a large surplus with Canada in finished goods manufacturing – including an almost perfectly balanced trade in autos and parts – and in services such as tourism or finance. One would think that Mr. Trump would not want to put these surpluses in jeopardy, which he certainly is doing by threatening to weaken Canada's economy and its considerable purchases of US manufactured goods and services.

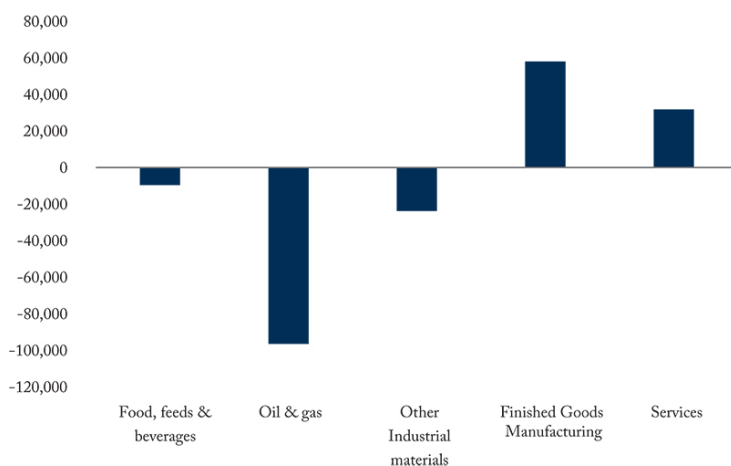
Canada is one of the United States' best customers, considering that the United States registers large deficits with most economies. Whereas globally the US exports 80 cents worth of goods and services for every dollar it imports, its exports to Canada are equivalent to 92 cents of what it imports from us, which stands in sharp contrast with the EU at 84 cents, Mexico at 69 cents, Japan at 65 cents, China including Hong Kong at 46 cents, etc.

Given these data, it may be concluded that Mr. Trump attacks Canada as he would other countries, precisely because it is so closely integrated with the United States, making it a more vulnerable or appealing economic target, amenable to politically valuable concessions on issues Mr. Trump cares about. Notably, he knows that the heightened costs and uncertainty he imposes on cross-border trade will favour businesses investing in the United States, the larger market, rather than in more vulnerable Canada.

Yet the US economy is also seriously vulnerable to disruption of trade with Canada. This will become evident soon enough in the form of higher consumer prices in the United States and in the very large and administratively costly number of requests by US businesses for relief from the tariffs. Canada's probable retaliation against US products will also highlight that reality.

Canada will have to rely on the US Congress, business community and the public to support overturning or reducing the tariffs, once they realize the negative impacts of the Trump tariffs on the US economy – and the fact that these measures will not improve the trade deficit and, by weakening one of their best customers while raising costs in the United States, may even worsen it.

Figure 1: United States Trade Balance with Canada:
Broad Sectoral Composition (Millions US\$, 2023)



Of course, if the name of the game is simply for Canada to suffer more than the United States, that is easy to achieve. But if the name of the game is to make Canada more eager to address US concerns such as those around dairy, digital, and cultural policies, ahead of the June 2026 planned review of the US-Canada-Mexico Agreement (if it survives), and more generally find ways to address US concerns with the balance of benefits from the trading relationship, then that can be done.

In addition to retaliating, which may help drive home the point in the United States but will also be costly to Canada, Canada needs to have a plan to increase its leverage in these negotiations, and ultimately for a future and less tumultuous trade relationship with the United States, one that also addresses Mr. Trump's concerns, whether legitimate or not.

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