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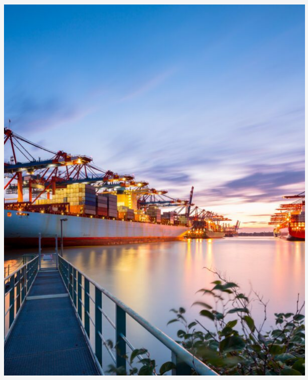
Past performance suggests future results: what a second Trump presidency means for Canadian trade



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As January approaches and, with it, a second Trump administration, Canadian businesses are bracing for uncertainty and discord with Canada's largest trading partner.

What will a second Trump presidency look like for Canadian businesses, and how might the government of Canada react?

1. Tariffs

Where past performance might be the clearest predictor of future policy is with respect to tariffs. The previous Trump administration invoked tariffs as a tool to protect American industries, reduce trade deficits, and leverage negotiations with other countries. Those tariffs targeted a range of goods, particularly from China, but also, and sometimes under the rationale of "national security", Canada, the European Union and other allies.

As a presidential candidate in 2024, President-elect Trump made 60% tariffs on Chinese goods and blanket tariffs of 10 to 20% on all other (non-Chinese) imported goods a centrepiece of his trade policy. There has been no indication yet that Canada would be exempt from these blanket tariffs.

Since approximately 80% of Canadian exports go to the U.S., this will be a critical issue for Canadian policymakers.

Moreover, U.S. court challenges during the first Trump administration affirmed the tariff-making discretion of the President under the authority delegated to him by Congress in various statutes, including the *Trade Expansion Act of 1962*, section 232 (relating to national security), and the *International Emergency Economic Powers Act* of 1977 (national emergencies and threats). A Republican-controlled Congress is unlikely to claw-back this authority, leaving the President's ability to impose tariffs largely unrestrained.

2. USMCA renegotiation

Renegotiation of the Canada-U.S.-Mexico Free Trade Agreement (USMCA) also looms. Formally, the USMCA is subject to review in 2026, but it is expected that the new administration will insist on a renegotiation of the agreement — possibly before 2026 — and backed by a threat of withdrawal from it, to address various issues of concern, some of which have also been raised by the Biden administration. These include reforms to the automotive rules of origin to discourage the use of Chinese parts and components in North American production, and the assembly of Chinese-brand vehicles in Mexico. Included as well are aspects of Canada's supply-managed agri-food sectors, particularly dairy, where U.S. dispute settlement challenges have been largely unsuccessful, and the repeal of Canada's digital services tax, which the U.S. considers to discriminate against its suppliers of digital streaming and other services.

Canada was able to secure most of its key trade interests quite effectively in the negotiations with the first Trump administration that produced the USMCA as a successor to the NAFTA. Its position will be more perilous and even more defensive in a new negotiation, as the new administration will be better prepared than the first Trump administration was in pursuing its mercantilist "America First" objectives, and less constrained both by domestic and diplomatic considerations in doing so.

3. Economic impacts on Canada

First, the economic uncertainty of moving from four decades of rules-based trade to chaotic and unilateral trade policies emanating from the U.S. will challenge businesses' supply chains and investment planning.

Second, Canadian industries that rely heavily on exports to the U.S. — and that is most of them — will almost certainly face increased costs and potential loss of market share as their goods may become less competitive compared to U.S. manufactured goods. This is speculative, however, and unlikely to be universal, given the complexity of global supply chains, and what will likely be exemptions from the tariffs, exchange rate effects, and other factors affecting supply decisions and prices. Beyond the direct economic effects, this may make weakened Canadian businesses more attractive targets for acquisition, or drive them to invest in the U.S. to hedge against increased business costs and reduced cross-border market access.

Third, Canadian efforts to better align with U.S. trade policy on China (of the sort we already have seen with surtaxes on Chinese electric vehicles and steel and aluminum goods) may mitigate some of the trade policy risks from south of the border, but at the cost of Chinese trade retaliation. We already have seen this play out in China's retaliatory dumping investigation into Canadian canola exports — a $6 billion export market for Canadian farmers and agricultural traders — in response to Canada's surtaxes on Chinese electric vehicles and steel and aluminum goods, which followed similar U.S. tariffs

4. Potential Canadian responses

If the new administration does impose tariffs on imports from Canada, our country will be compelled to respond in kind against U.S. imports, as it did in response to the first Trump administration's section 232 tariffs on Canadian steel and aluminum. Canadian officials and businesses will need sustained engagement with their U.S. counterparts, particularly in areas of the U.S. that will be economically sensitive to Canadian trade retaliation and/or which depend on Canadian inputs. These include businesses in states in the Great Lakes region, California, and those that depend on Canadian energy imports.

Canada can possibly improve trade relations and strengthen its economic ties with other trading partners who will be in the same position vis-à-vis the U.S., such as the European

Union, Japan and South Korea. Historically, Canadian efforts to diversify trade and reduce its dependency on the U.S. have mostly failed and have suffered from lack of sustained ambition and commitment. However, the breakdown of enduring assumptions about the reliability and dependability of the U.S. as a trading partner may create a new impetus to expand Canadian access to other markets, one that may have a better chance of overcoming the gravitational pull of Canada’s closest and wealthiest neighbour.

There is also likely to be political pressure in Canada for support measures to help workers and businesses adversely affected by U.S. tariffs or by a broader trade war. To the extent that such support takes the form of subsidies, it will risk further challenges from Canada’s trading partners, including the U.S. itself.

Conclusion

Canada will not be the only country adversely affected by a shift in U.S. trade policy. However, Canada’s uniquely close economic ties with, and export dependency on, the U.S. make it particularly vulnerable. That vulnerability is exacerbated by its traditional negative net foreign investment balance and the growing gap between Canadian direct investment outflows to the U.S., and U.S. investment inflows into Canada. In the face of this challenge, Canadian businesses should draw on their experiences in the first Trump presidency and be prepared to navigate through even stormier years ahead.