ECONOMIC VIEWPOINT

Having Truck and Trade with the Good Ole US of A

Which Provinces Are Most Exposed to Potential US Tariffs?

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HIGHLIGHTS

- With the Republican sweep of the presidency and Congress now confirmed, higher tariffs are widely expected. This has weighed heavily on our economic outlook for Canada.
- But Canadian provinces are highly diverse in their economic drivers, and some will be more vulnerable to US tariffs than others. For instance, we expect energy products to be largely exempt from tariffs, which would be a lucky break for Alberta, Saskatchewan, and Newfoundland and Labrador. As a centre of oil refining, New Brunswick may also be spared the worst ravages of higher tariffs.
- With their highly diversified economies and close ties to the US market, Ontario, Quebec and Manitoba may not be so lucky. The same is true, albeit to a lesser extent, for British Columbia, Nova Scotia and Prince Edward Island.
- While diplomacy may help to carve out some tariff exemptions, the most important takeaway from the latest round of US-driven global trade dysfunction on the horizon is that trade diversification is key to mitigating the risks of any one country's policies.

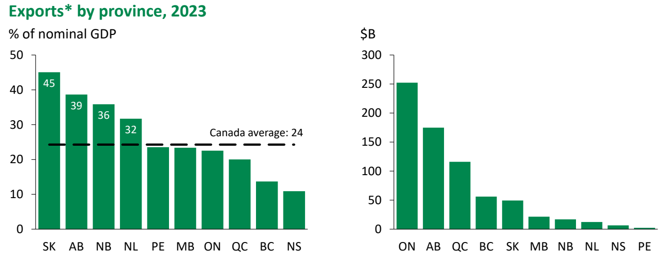
With the Republican sweep of the presidency and Congress now confirmed, President-elect Donald Trump will have few impediments to implementing his policy agenda. As we outlined in our latest *Economic and Financial Outlook*, this will have meaningful implications for Canada's economy, most of them negative. The biggest hit will come from the proposed 10%, possibly 20%, tariff on all US imports.

But Canada is a big, diverse country. Each of its ten provinces has distinct economic drivers and trade relationships with other countries, particularly the US. And it's those differences that make some provinces more exposed than others to proposed US tariffs.

Energy Exports Are Expected to Avoid US Tariffs

Starting with industries that are likely to be least exposed to new and expanded US tariffs, our preelection analysis determined that the energy sector is chief among them. That's because President-elect Trump has committed to bringing down gasoline prices, so any measure that works against that will probably be avoided. That's good news for Alberta, Saskatchewan, and Newfoundland and Labrador (graph 1). Indeed, we expect the Trans Mountain pipeline expansion to continue supporting growing production and exports of crude oil from Wild Rose Country for the foreseeable future.

Graph 1
Energy-Producing Provinces Export Most as a Share of GDP

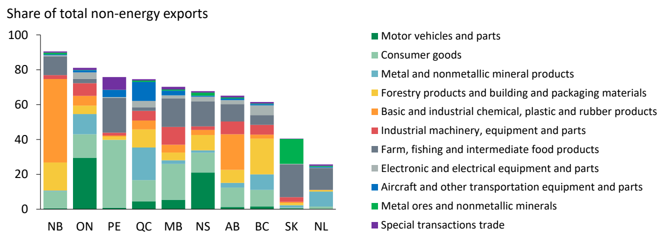


* Domestic exports, excluding re-exports.
Statistics Canada and Desjardins Economic Studies

New Brunswick may also escape the worst ravages of the Trump tariffs, as refined petroleum and coal products make up the lion's share of its exports to the US (graph 2). Grouped in with basic and industrial chemical, plastic and rubber products, they make up the second-largest export category in Alberta as well. However, with forestry products a common target for US trade penalties, Canada's only officially bilingual province may not be able to avoid tariffs entirely. The same is true for British Columbia (BC).

Graph 2
Refined Fuel Exports Drive Non-Energy Exports in New Brunswick

Provincial non-energy exports* to the US, 2023



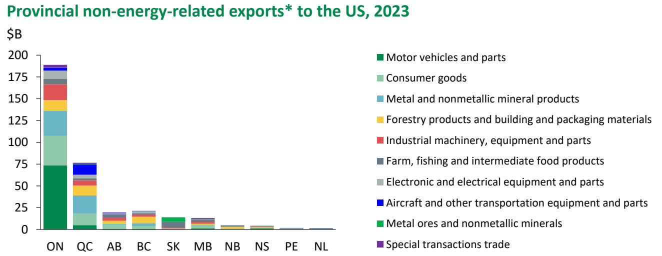
* Domestic exports, excluding re-exports.
Statistics Canada and Desjardins Economic Studies

Non-Energy-Related Exports May Not Be So Lucky

Setting energy and chemical exports aside (the latter of which include refined petroleum and coal products) gives a better sense of which provinces are most exposed to prospective US tariff hikes. Ontario tops the list as the source of more than half of Canada's non-energy-related exports (graph 3). Indeed, the export value of motor vehicles and parts from Ontario alone was almost as substantial in 2023 as all of Quebec's non-energy-related exports combined. It is possible, however, that the automotive industry could be exempt from a possible tariff increase. This is a highly integrated industry in North America with very close trade ties. According to the Canadian Vehicle Manufacturers' Association, "parts and components may cross Canadian-U.S.-Mexican borders as many as 8 times before being installed in a final assembly." This industry has benefited from some form of free trade since the 1960s, well before the first free trade agreement between Canada and the United States. Under these conditions, the imposition of customs tariffs could have significant multiplier effects on the prices of motor vehicles produced not only in Canada but also in the United States, which the new American administration may want to avoid.

Graph 3
Ontario Exports More than Half of Canada's Non-Energy-Related Goods

Provincial non-energy-related exports* to the US, 2023

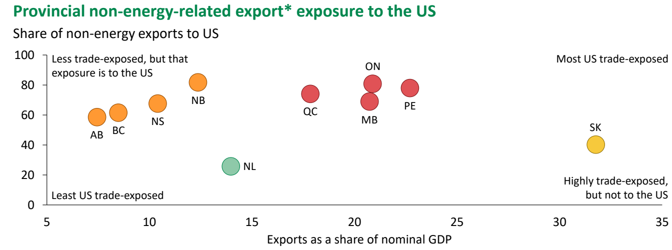


* Domestic exports, excluding re-exports; non-energy-related exports exclude energy and chemicals, the latter of which are primarily composed of petroleum and coal products.
Statistics Canada and Desjardins Economic Studies

But as Canada's second-largest exporter of metal and nonmetallic mineral products to the US, Quebec is also highly vulnerable to US tariffs. It felt the sting of 10% levies on aluminum during the prior Trump administration in 2018 (while Ontario was hit with 25% tariffs on steel). The aerospace sector is also vulnerable, as are the forestry and consumer goods industries. Due to the significant integration of supply chains in Canada and the United States in the aeronautics industry, it is also possible that the latter will be exempt from a possible tariff increase. Concerns have been expressed about the possible tariff treatment of Quebec's agricultural exports as well. For that reason, La Belle Province is lumped in with the other highly diversified provincial economies of Ontario and Manitoba in being particularly exposed to US tariffs (graph 4).

Graph 4
Ontario, Manitoba and Quebec Are Highly US Trade-Exposed

Provincial non-energy-related export* exposure to the US



* Domestic exports, excluding re-exports; non-energy-related exports exclude energy and chemicals, the latter of which are primarily composed of petroleum and coal products.
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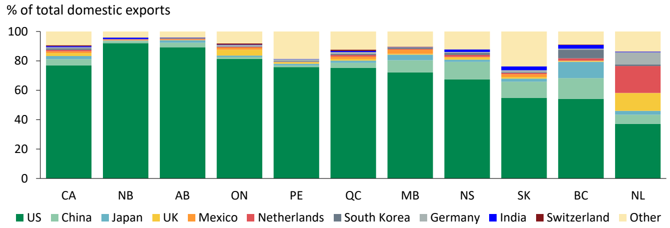
Manitoba is an exception among the Prairie provinces. While exports of farm, fishing and intermediate food products to the US make up a notable share of its overall trade, its economy is quite diverse. Exports to the US are driven by consumer goods, and to a lesser extent industrial machinery, equipment and parts. And while Saskatchewan exports a similar share of foodstuffs to the US, where it stands in contrast is its exports of metal ores and nonmetallic minerals, such as potash. Saskatchewan also exports the least to the US as a share of its total non-energy-related exports among Canadian provinces, save for Newfoundland and Labrador and British Columbia. Indeed, compared to their Canadian peers, these three provinces have highly diversified export destinations (graph 5). This is a strategy for mitigating the export risks we focused on in our recent report on trade and small business in Canada.

Graph 5
Saskatchewan, BC, and Newfoundland and Labrador Export Relatively Less to the US
Exports* by trade partner, 2023



* Domestic exports, excluding re-exports.
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The Atlantic provinces are unique in and of themselves. Prince Edward Island (PEI) is especially exposed to US tariffs on non-energy-related exports such as consumer goods, farming and fishing. The fishing industry could be vulnerable across all the East Coast provinces. Notably, Nova Scotia stands out as a Maritime province with an economy that is particularly diverse and linked to the US, having motor vehicles and parts as its leading category of exports destined for south of the border.

Tariffs Will Leave US Consumers Much Worse Off

Fortunately for Canadian exporters, a 10-20% tariff is expected to be applied across the board (except for China, which could purportedly be subject to a 60% tariff). That means it will be difficult for American companies to substitute imports from other countries in place of those from Canada. Consequently, costs will get passed on to US consumers as opposed to leading to a more substantive reduction in Canadian exports.

The hope seems to be that higher tariff-induced domestic inflation will lead some businesses to increase domestic production stateside. But research by the US Federal Reserve (2019) found that "U.S. manufacturing industries more exposed to tariff increases experience relative reductions in employment[,] as a positive effect from import protection is offset by larger negative effects from rising input costs and retaliatory tariffs." As such, Americans can expect short-term pain for uncertain long-term gain.

Conclusion

While we have yet to release our updated provincial economic outlook, these results suggest impending tariffs could weigh most heavily on Ontario, Quebec, Manitoba and PEI going forward. Nova Scotia and BC may not be too far behind. Meanwhile, Alberta, Saskatchewan, Newfoundland and Labrador, and New Brunswick could be spared the worst of the Trump tariffs. This is thanks in part to the importance of crude oil and refined petroleum products in those provinces. But they have other lessons to offer besides just being blessed with energy riches. Saskatchewan and Newfoundland and Labrador have particularly diverse destinations for their exports, leaving them less exposed to the whims of politicians in any one country. Canadian policymakers have been trying to encourage greater trade diversification for decades but with little success. Maybe another four years of US-driven trade dysfunction will help to make the case.