ECONOMIC VIEWPOINT

Tit for Tat: What Do Retaliatory Tariffs Mean for Canadian Imports, Growth and Inflation?

By LJ Valencia, Economic Analyst, and Randall Bartlett, Deputy Chief Economist

- To get a sense of how the retaliatory tariffs will affect the Canadian economy, it's important to dig into the details. Namely, which imported goods will tariffs be applied to, and how significantly will price changes impact demand for those goods?
- Looking at the federal government's lists of targeted goods, there doesn't seem to be a clear strategy of largely applying tariffs to just those imports that Canadians can easily substitute with similar goods produced at home or abroad. Instead, other selection criteria were also used, such as the impact on US exporters or reciprocity of tariffed goods on both sides of the border. As a result, the 25% tariffs on select imports from the US should broadly translate to an eventual 25% reduction in demand.
- Due to the size of the actual and proposed counter tariffs and the types of imported goods they apply to, inflation in Canada could be about 0.6 percentage points higher over the next year than it would be otherwise. It would be even higher if not for the drag on real GDP from the tariffs on both sides of the border. However, it's important to note that Canada would be hard pressed to avoid a recession because of the trade war, even if it decided not to apply retaliatory tariffs.

As Desjardins Economic Studies has previously outlined, retaliatory tariffs are likely to squeeze many industries that are also going to be hit by US import tariffs and a weakened Canadian dollar. However, demand for different imported goods isn't equal. Some may be substituted more easily than others, whether for goods produced domestically or further abroad. With that in mind, this report:

- Outlines the criteria that may be considered when determining which imported goods should be hit with retaliatory tariffs;
- Examines the Government of Canada's lists of goods that are, or could be, subject to counter tariffs;
- Looks at how sensitive demand for those goods is to price changes; and
- Explores the potential impacts on growth and the prices paid by Canadians.

Considerations When Applying Retaliatory Tariffs

There are four broad criteria that the Government of Canada seems to be considering when applying retaliatory tariffs to US imports. The first is the impact that those tariffs will have on US exporters, particularly those in specific geographic regions. This is the case for Florida orange juice and Kentucky bourbon, for example. Second is the impact the tariff will have on the Canadian economy: The more easily Canadians can find substitutes for a specific good, the lower the impact that tariff will have on growth and inflation. Third, reciprocity matters, such as putting tariffs on imports of US steel and aluminum after the United States did the same to Canada. And fourth, the government is ensuring that the impact of counter tariffs isn't regionally concentrated, so as not to disproportionately place the burden on one part of the country over another.

What's Getting Hit with Retaliatory Tariffs?

The federal government published a long list of imported goods that have been or could be hit with retaliatory tariffs of 25%. These goods number in the thousands, and range from umbrellas to underwear and steel to spirits. The full list of counter-tariffed goods was released in three waves: $30B of imported goods on March 4, 2025; another $30B of goods imports on March 13, 2025; and a remaining $125B in Canadian imports from the US yet to have tariffs applied.

In total, the full list of imported goods from the US that could be subject to Canadian tariffs has reached $185B. To put this number in perspective, Canada imported $377B in goods from the US in 2024. That means more than 50% of our imports from the US may now be subject to an additional import tariff. And since tariffs are paid by the households and businesses of the country that applied them, Canadians will feel it on their bottom lines.

That begs the question: What specific goods are getting hit with retaliatory tariffs? To boil it down to something more digestible, we've taken the thousands of goods on each list and classified them according to their "HS2" codes—the first two digits of their Harmonized System of trade codes. These 96 categories cover every type of product that is imported or exported.

In the first $30B wave of goods that were subject to counter tariffs on March 4, the largest share of impacted imports was cosmetics (table 1), followed by paper products and nuclear reactors, boilers, machinery and mechanical appliances and parts.[1] Rounding out the top five impacted import categories are rubber and wood products. This increased the effective tariffs on US imports by about 1.8 percentage points (ppts).

Table 1
Top Ten Import Categories from the Initial $30B Retaliatory Tariff List

	HS CODE & DESCRIPTION	2024 TOTAL ($B)	IMPORT ELASTICITY (WEIGHTED SUM)
1	33 - Essential oils and resinoids; perfumery, cosmetic or toilet preparations	2.9	-0.97
2	48 - Paper and paperboard; articles of paper pulp, of paper or of paperboard	2.5	-0.90
3	84 - Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	2.3	-0.96
4	40 - Rubber and articles thereof	2.1	-0.72
5	44 - Wood and articles of wood; wood charcoal	2.0	-0.33
6	94 - Furniture; bedding, mattresses, mattress supports, cushions, etc.	1.8	-0.81
7	39 - Plastics and articles thereof	1.7	-1.00
8	22 - Beverages, spirits and vinegar	1.7	-0.91
9	71 - Natural or cultured pearls, precious or semi-precious stones, etc.	1.3	-0.95
10	21 - Miscellaneous edible preparations	0.8	-1.00

These are matched elasticities, weighted by nominal export shares for 2024. Elasticities are based on M. Ghodsi, J. Grübler and R. Stehrer, "Import Demand Elasticities Revisited," wiiw Working Paper, No. 132.
Statistics Canada, Vienna Institute of International Economic Studies and Desjardins Economic Studies

In response to US tariffs on Canadian steel and aluminum, Canada also imposed highly targeted retaliatory tariffs on the same goods on March 12 (table 2). But imports of those goods only make up about half of the $30B response, leading to a more expansive list of tariffed goods. That's similar to the 2018 response to US tariffs on the same products. This further increased the effective tariffs on US imports by about 1.4 ppts.

Table 2
Top Ten Import Categories from the Latest $30B Retaliatory Tariff List

	HS CODE & DESCRIPTION	2024 TOTAL ($B)	IMPORT ELASTICITY (WEIGHTED SUM)
1	73 - Articles of iron or steel	7.1	-0.92
2	71 - Natural or cultured pearls, precious or semi-precious stones, etc.	7.0	-0.19
3	72 - Iron and steel	5.5	-1.03
4	76 - Aluminum and articles thereof	3.0	-0.98
5	94 - Furniture; bedding, mattresses, mattress supports, etc.	1.4	-0.04
6	85 - Electrical machinery and equipment and parts, etc.	1.4	-0.26
7	83 - Miscellaneous articles of base metal	1.2	-0.97
8	84 - Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	1.1	-0.95
9	95 - Toys, games and sports requisites; parts and accessories thereof	0.9	-0.72
10	82 - Tools, implements, cutlery, spoons and forks, of base metal, etc.	0.8	-0.96

These are matched elasticities, weighted by nominal export shares for 2024. Elasticities are based on M. Ghodsi, J. Grübler and R. Stehrer, "Import Demand Elasticities Revisited," wiiw Working Paper, No. 132.
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On April 3, the federal government announced it would be matching the latest US duties with 25% tariffs on all vehicles imported from the United States that are not compliant with the Canada-United States-Mexico Agreement (CUSMA). However, unlike the US tariffs, Canadian duties will not affect auto parts. By our estimate, this could increase the effective tariff rate on Canadian imports from the US by as much as 0.4 ppts. That takes the total increase in the effective tariff rate on Canadian imports from the US to around 3.5 ppts since the start of the year.

That leaves the remaining $125B of goods that could be slapped with counter tariffs (table 3). But since the final list covers more than $125B in imports, a 21-day public comment period is being held to winnow it down before implementation. As such, what's on this list remains uncertain. But looking at what's covered by this extensive list, tariffs could potentially be applied to product categories such as vehicles other than railway or tramway rolling-stock (things like golf carts, tractors, wheelchairs and strollers), plastics products, and nuclear reactors, boilers, machinery and mechanical appliances and parts. If the federal government proceeds with applying a 25% tariff to this final list of $125B in imports from the US, the total increase in the effective tariff rate could reach roughly 12.5 ppts on top of where it ended 2024.

Table 3
Top Ten Import Categories from the Remaining $125B List

	HS CODE & DESCRIPTION	2024 TOTAL ($B)	IMPORT ELASTICITY (WEIGHTED SUM)
1	87 - Vehicles other than railway or tramway rolling-stock, etc.	52.8	-0.77
2	39 - Plastics and articles thereof	16.3	-0.91
3	84 - Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	16.2	-0.92
4	85 - Electrical machinery and equipment and parts	14	-0.62
5	73 - Articles of iron or steel	7.3	-0.92
6	71 - Natural or cultured pearls, precious or semi-precious stones, etc.	7.1	-0.18
7	72 - Iron and steel	5.9	-1.04
8	48 - Paper and paperboard; articles of paper pulp, of paper or of paperboard	5	-0.57
9	30 - Pharmaceutical products	4.4	-0.98
10	76 - Aluminum and articles thereof	4.1	-0.99

These are matched elasticities, weighted by nominal export shares for 2024. Elasticities are based on M. Ghodsi, J. Grübler and R. Stehrer, "Import Demand Elasticities Revisited," wiiw Working Paper, No. 132.
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[1] Nuclear reactors and parts are excluded from the retaliatory tariffs in the nuclear reactors, boilers, machinery and mechanical appliances parts products (HS84) category.

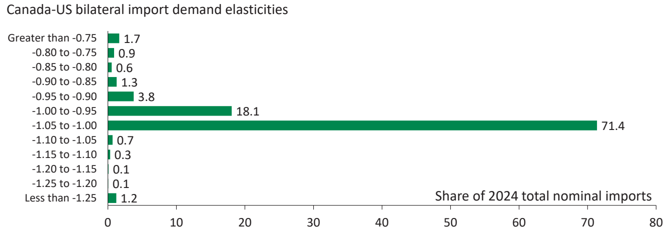
What Goods Are Canadians Most Likely to Find Substitutes For?

However, not all imports are created equal. Even if the same import tariff is applied across the board, Canadians may continue purchasing some goods while leaving others on the shelf. This is particularly true in the current trade dispute, since the Government of Canada is applying these tariffs exclusively to imports from the United States, not its other trading partners.

For imported goods, a change in price will lead to a change in demand. Economists refer to this as *import demand elasticity*. While these elasticities can vary significantly for different types of imports, they are generally around a value of -1 for imports from the US, meaning a 25% tariff leads to an eventual 25% decline in demand for the tariffed good (graph 1). The more negative the number, the more sensitive that demand is to changes in import prices—meaning Canadians are likelier to find a substitute when the price goes up. The opposite is true, as well. If import demand elasticity is close to zero, as is the case for refined petroleum products, demand is less likely to be affected by changes in prices. As a result, tariffs on these goods could have a more negative impact on growth while pushing up inflation. More specifically to our analysis, we're using *bilateral import demand elasticities*, which measures the impact that price changes for US goods imports will have on Canadian demand.

Graph 1
Canadian Import Demand Elasticities for US Exports Are Close to -1

Import demand elasticities by share of nominal imports
Canada-US bilateral import demand elasticities



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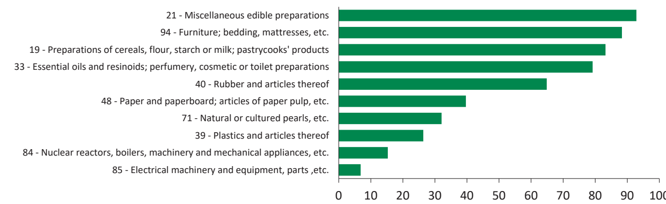
Looking at the first list of $30B in tariffed goods imported from the US, we expected to find a bias toward goods that have more elastic import demand (that is, a more negative elasticity), meaning Canadians could substitute them more easily. However, the weighted-average import demand elasticity of these goods is instead close to the economy-wide average of -1. In aggregate, this suggests that overall Canadian demand for these goods should ultimately fall broadly in line with the extent of the 25% import tariff applied.

But where this list does distinguish itself is in the impact it is likely to have on US exporters. Canada is a major market for the US exports included in this first list of counter-tariffed goods (graph 2). Items that top the list include prepared foods, furniture and furnishings, cosmetics, and rubber products. In all of these cases, more than 60% of total US exports were destined for Canada in 2024.

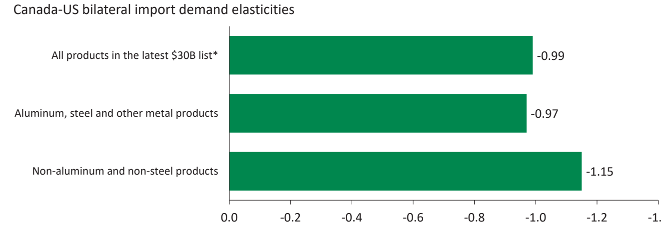
Graph 2
The Initial $30B List of Tariffed Imports Is Targeted at Key US Export Sectors
Tariffed US exports to Canada as share of overall US exports by category, 2024
% of total US exports by HS2 export category



Items are matched at the HS 4 level; nominal shares could be lower than presented.
International Trade Administration and Desjardins Economic Studies

The second $30B list of goods hit with retaliatory tariffs also has a weighted-average import demand elasticity that is close to the national average. This doesn't come as much of a surprise: in the spirit of reciprocity, this list targets mainly steel and aluminum, both of which have been subject to tariffs on the US side. However, the remaining impacted goods imports (excluding aluminum and other steel products) have a weighted-average import elasticity of approximately -1.2, meaning they are more easily substituted with goods produced elsewhere than the imports in the first $30B retaliatory list (graph 3). Notably, the subsequently increased tariffs on auto imports from the US were similarly reciprocal in nature, hence its less negative import demand elasticity of -0.75.

Graph 3
Aside from Aluminum and Steel, the Remaining Imports on the Latest $30B List Are More Easily Substituted
Import demand elasticities (weighted average)
Canada-US bilateral import demand elasticities



* Refers to the list of counter-tariffed goods published on March 13, 2025
Statistics Canada, Vienna Institute of International Economic Studies and Desjardins Economic Studies

Finally, there is the remaining $125B in soon-to-be-tariffed goods. The larger group that these goods will be selected from has a more negative weighted-average import demand elasticity than the average for all of the economy's imports, taken as a whole (table 4 on page 4). That means demand for these goods is more elastic, and there is an opportunity to minimize the impact of these retaliatory tariffs by favouring goods that Canadians can more easily substitute with goods produced at home or abroad—i.e., the ones with the most negative demand import elasticity. These include, but are not limited to, goods such as textiles, grains, dairy and meat.

Table 4
The Long List of Potentially Counter-Tariffed Imports Has More Goods That Can Be Substituted with Other Products

CATEGORY	IMPORT ELASTICITY (WEIGHTED AVERAGE)	IMPORT ELASTICITY (SIMPLE AVERAGE)
$30B Tariff Table (Mar. 4, 2025)	-0.99	-0.97
$30B Retaliatory Tariffs (Mar. 13, 2025)	-0.99	-1.00
$125B Exploratory List Ex-Retaliatory Tariffs	-1.03	-1.03
Economy-Wide	**-0.99**	**-1.04**

These are matched elasticities, weighted by nominal export shares for 2024. Elasticities are based on M. Ghodsi, J. Grübler and R. Stehrer, "Import Demand Elasticities Revisited," wiiw Working Paper No. 132.
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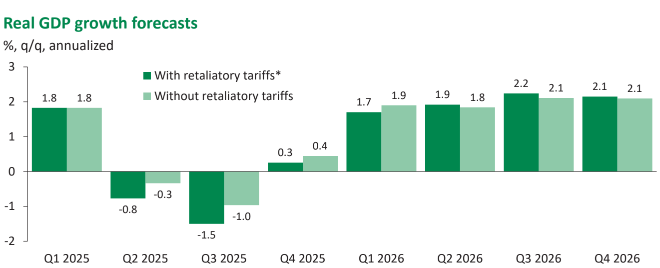
What Do Retaliatory Tariffs Mean for Growth and Inflation?

With this latest tariff information, we can update the forecast from our most recent Economic and Financial Outlook. We've estimated that if counter tariffs of 25% are applied to $185B in imports within the next month, the level of real GDP would be lower by about 0.3% at its peak drag by the end of 2025. That said, while avoiding retaliatory tariffs might ease the pain for Canadians, it is likely insufficient to stave off a recession (graph 4). We also assume that US tariffs will be scaled back from 25% to 10% in early 2026 (0% for energy), and that tariffs should similarly be reduced on the Canadian side of the border. That would mitigate the long-term damage compared to the prolonged 25% tariff scenario, although not offset it entirely.

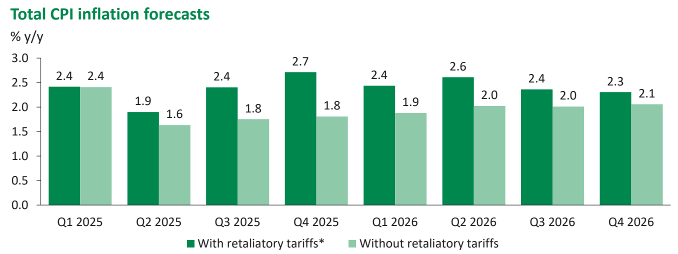
Graph 4
Canada Would Likely Experience a Recession Without Retaliatory Tariffs



*Refers to the real GDP growth forecast published in our March 2025 Economic and Financial Outlook, revised for Canadian tariff announcements up to and including April 3, 2025.
Desjardins Economic Studies

Turning to inflation, it should come as no surprise that retaliatory tariffs will increase the prices Canadians pay. By our estimate, counter tariffs could increase inflation for the year starting in Q2 2025 by 0.6 percentage points, to 2.4% y/y, if the retaliatory tariffs on the remaining $125B in goods imports kick in before the end of the quarter (graph 5). Notably, the sharp increase in import prices will be partly offset by the disinflationary pressure coming from a weaker economy. It will also be mitigated somewhat by the ability of US and Canadian companies to pass on those price increases. Our revised Canadian dollar outlook, which now calls for less depreciation against the greenback than previously expected, implies that inflationary effects may be more limited as well. And as we noted recently, inflation would likely have been even higher over the next year—topping 3% y/y—had the federal consumer carbon tax not been eliminated.

Graph 5
Total Inflation Would Be Lower Without the Retaliatory Tariffs



*Refers to the CPI inflation forecast published in our March 2025 Economic and Financial Outlook, revised for Canadian tariff announcements up to and including April 3, 2025.
Statistics Canada and Desjardins Economic Studies

Normally, higher inflation would elicit an increase in interest rates by the Bank of Canada. However, given the nature of the inflationary shock, we are of the view that the Bank of Canada will continue to gradually cut the overnight policy rate, ending 2025 at 1.75%. This should help to offset some of the economic damage caused by tariffs and counter tariffs, albeit very modestly.

Conclusion

Retaliatory tariffs are supported by most Canadians and may be a logical choice, in terms of pressuring the US administration to remove their own tariffs on imports from Canada. But this move won't come without consequences. Tariffs will push up inflation and result in weaker growth. This risk is exacerbated by the list of goods being hit with retaliatory tariffs. They weren't just selected to minimize the stagflationary shock to the Canadian economy, but also to maximize the hit to US exports. It's a difficult balance to strike, particularly when recognizing the need for reciprocity and regional fairness. Thus far, the Government of Canada seems to have done as good a job as one might hope for. We hope that thoughtful approach continues going forward.