

Trump Redux and the Canadian-American Trading Relationship

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In his first run for the presidency, Donald Trump campaigned on tearing up the 1994 North American Free Trade Agreement (NAFTA) among Canada, Mexico, and the United States. In office, President Trump subsequently negotiated and signed a new trade agreement with Canada and Mexico that kept intact the largely barrier-free trade and investment bloc among the three partners and created opportunities for their greater economic integration. President Trump described the 2020 United States, Mexico and Canada Agreement (known as USMCA in the US and as CUSMA in Canada) as “the largest, fairest, most balanced and modern trade agreement ever reached.”¹

Four years later, Trump’s threat to levy a 25% tariff on imported goods from Canada and Mexico on his first day in office belie his own praise for CUSMA. His declaration that the 25% tariff will be maintained “until such time as Drugs, in particular Fentanyl, and all Illegal Aliens stop this Invasion of our Country”² has once again engendered uncertainty in the Canada-American trading relationship. Even if the issue of illegal cross-border traffic in drugs and migrants is resolved, the persistent jeopardy to Canada over Trump’s four-year presidential term will be his ‘America First’ ambition: that is, to (re-)domicile production and investment in the US and away from other countries, and to use the threat and/or imposition of tariffs and other protectionist measures to do so.

The discussion which follows addresses the Canadian government’s response to date, in the run-up to Trump’s January 20th inauguration, to the 25% tariff threat, and reflects on the challenges confronting Canada in its trading relationship with the US and the Trump administration over the next four years.

Canadian governments—federal and provincial—have no option but to take seriously Trump’s 25% tariff threat because access to the US market is critical to Canada’s economy. Almost 80% of Canadian exports go to the US and foreign direct investment (FDI) from the US accounts for

almost one-half of all Canadian FDI.³ The tariff would be especially damaging to Canada's energy, automotive, and manufacturing sectors but the entire Canadian economy would take a hit. It is estimated that a 25% US tariff would cause Canada's GDP to shrink by a 2-3 percent (depending upon if and how Canada retaliates) and push Canada into a recession by mid-2025.⁴

In an effort to avoid these potentially dire consequences, the Canadian government has responded with both policy and diplomatic actions. Policy-wise they have sought to deal with the problems that Trump pointed to in his tariff threat: the flow of illegal drugs and migrants into the US. While stressing that it is Mexico, not Canada, that is overwhelmingly the source of the latter problems for the US, the Canadian government has nonetheless acknowledged Trump's concern. It unveiled a \$1.3 billion plan in December 2024 to secure the Canada-US border. The plan entails new tools for law enforcement that include a proposed aerial surveillance task force, helicopters, drones and mobile surveillance towers between ports of entry; enhanced coordination with US law enforcement; increased information sharing and limiting traffic at the border; increased funding to the Canada Border Service Agency to train new dog teams to find illegal drugs and new detection tools for high-risk ports of entry.⁵

Diplomatic efforts have entailed separate visits by Prime Minister Trudeau and subsequently his Finance and Foreign Affairs ministers. These visits were an attempt to secure a Canadian exemption from the pending tariffs, and to emphasize the benefits of CUSMA to the US, the deep integration of the US and Canadian economies, and the consequent damage to the US economy were tariffs imposed on Canadian goods entering the US.⁶ These missions to Mar a Lago failed to elicit a carve-out commitment from Trump for Canada.

The threat of retaliation in the event President Trump does implement tariffs on Canadian goods has also been put on the table by Canadian federal politicians and the premier of Canada's largest province, Ontario.⁷

It should become clearer after Trump takes office on January 20th whether his 25% tariff threat is specific to the issue of curtailing illegal migrant and drug traffic into the US. As such a negotiating ploy, Trump could declare victory for having leveraged Mexican and Canadian government actions on the issue and decide to remove or delay the actual tariffs.

There are, however, reasons to be apprehensive that the threat and/or imposition of tariffs will be a recurrent mode of operation and feature of Trump's trade policy over his four-year term. Trump has made it clear that he doesn't believe trade liberalization is working for Americans. Moreover, he sees import tariffs and other protectionist measures as a means to correct that situation by encouraging reshoring of American manufacturing and generating revenues to pay for tax cuts and spending.⁸ This ideology is shared by economic advisors within his inner circle.⁹

The situation facing Canada over the next four years of the Trump Presidency is thus highly worrisome for the country. Canada can expect tariffs (or, minimally, their threat) to be wielded as a preferred instrument of US trade policy. It can expect to be at the receiving end of aggressive US attempts, including through use of its asymmetrical market power, to make concessions that reflect Trump's zero-sum approach to international trade.¹⁰ Canada will be under pressure to deal with a handful of US trade irritants during, if not before, the review and renegotiation of

CUSMA in 2026. They include issues that were not resolved to the US's satisfaction in CUSMA or subsequently by its dispute settlement bodies (such as Canadian dairy and auto parts policies), as well as issues that have since arisen (such as taxes on large digital service providers, most of whose headquarters are in the US).¹¹

Canada's hand in negotiations on such matters and in the CUSMA review will be stronger if it is able to replicate the strategy adopted by the Liberal government throughout the 2017-19 NAFTA renegotiations. Its Team Canada approach then brought representatives of all federal political parties as well as the provinces, cities, business, labour and other civil society groups into federal consultations throughout the negotiations. It proved successful in securing considerable consensus inside Canada on Canada's strategy. Members of Team Canada, as well as the provinces, mounted a vigorous communications and information campaign with their US counterparts, conveying the importance and economic benefits of the Canadian-American trading relationship to every US state and Congressional district. At the negotiating table, Canadian negotiators were assertive in defending what they saw as Canadian interests. They were also prepared to retaliate when, amidst stalled negotiations, Trump imposed tariffs in June 2018 on Canadian steel and aluminum and threatened tariff on Canadian cars. In return, Canada implemented dollar for dollar tariffs on goods produced in Republican-leaning states. Trump later ended the tariffs without concessions from Canada.

While there is consensus that a united—Team Canada—approach is again needed to deal with the trade threats posed by the incoming Trump administration, the Canadian political context over the next year will confound this task. During the 2017-19 NAFTA renegotiations, the government of Canada enjoyed a parliamentary majority. In contrast to the political stability of that period, 2025 will be marked by political change. Subsequent to Prime Minister Trudeau's January 6th announcement of his resignation, the Liberal Party will undergo a search for his successor over the next three months. Canada will face an election--no later than October 20th, but possibly as early as this spring—that current polls indicate will result in a change to a Conservative government in Ottawa. Forging a coherent Canadian negotiation strategy will also be hampered by visible differences across provinces on the respective roles of concessions and retaliation (counter-tariffs) to deal with American tariff threats.¹²

This domestic political context will not, however, inhibit use of another plank in the Canadian 2017-19 trade negotiation strategy. It is a concerted and continuing informational and lobbying campaign by Canadian political, business, and labour leaders centered on two messages to their US counterparts. One is the benefits to them of CUSMA. The other is the benefits to them of a rules-based trading system and the costs to them of their country violating the terms of trade agreements (by, for example, levying tariffs illegal under CUSMA) that their country has signed. Mitigating the deleterious impacts for Canada of Donald Trump's America First agenda is likely to depend, in no small measure, on American voters' receptivity to both messages.

¹ As quoted in Ana Swanson and Emily Cochrane, Trump Signs Trade Deal with Canada and Mexico, *New York Times*, January 29, 2020.

<https://www.nytimes.com/2020/01/29/business/economy/usmca-trump.html>

² Reuters, “Trump promises 25% tariff on products from Mexico, Canada in 2024.” November 25, 2024. The words in quotes are as posted by Trump on his Truth Social.

³ See the website of Global Affairs Canada: <https://www.international.gc.ca>

⁴ Stephen Tapp and Trevor Tombe, What the Return of the “Tariff Man” Means for the Canadian and U.S. Economies. Business Data Lab. November 28, 2024.

<https://businessdatalab.ca/publications/what-the-return-of-the-tariff-man-means-for-the-canadian-and-u-s-economies/> These estimates assume the consequences of the tariff would include job losses, companies moving production from Canada to the US, the value of the Canadian dollar declining vis-à-vis the US dollar and rising inflation in Canada.

⁵ Marie Woolf, Ottawa outlines border-reinforcement plan, *The Globe and Mail*, December 18, 2024.

⁶ See the analyses of Trevor Tombe, Partners in Prosperity: Exploring the Significance of Canada-U.S. Trade for the Canadian Chamber of Commerce’s Business Data Lab, October 2024.

https://businessdatalab.ca/wp-content/uploads/2024/10/PartnersInProsperity_EN_Final.pdf

Analyses of the damage to the US economy of the tariffs is also being produced by US-based institutions like the Peterson Institute of International Economics. See, for example, Julieta Contreras, Mary E. Lovely and Jing Yan, “No trade tax is free: Trump’s promised tariffs will hit large flows of electronics, machinery, autos and chemicals. December 12, 2024.

<https://www.piie.com/blogs/realtime-economics/2024/no-trade-tax-free-trumps-promised-tariffs-will-hit-large-flows>

See also National Institute of Economic and Social Research. Trump’s Tariffs: A Trade Gamble with Mexico and Canada. December 11, 2024. <https://niesr.ac.uk/blog/trumps-tariffs-trade-gamble-mexico-and-canada>

⁷ Steven Chase and Laura Stone, “Ford floats halt on energy exports to U.S.” *The Globe and Mail*, December 12, 2024; Steven Chase, Laura Stone and Kelly Cryderman, “Canada weighs export tax to counter Trump tariff pledge,” *The Globe and Mail*, December 13, 2024.

⁸ Douglas A. Rediker, “The Consequences of Trump’s Tariff Threats,” December 11, 2024. Brookings. Rediker elaborates: “Under this approach, tariffs are either assumed to be ‘costless,’ with no negative impacts borne by domestic consumers (through higher prices) or by businesses (through higher-priced inputs and disrupted supply chains), or that tariffs might increase consumer prices, but that is a price worth paying in order to revive the American industrial base.”

⁹ One such advisor is Peter Navarro who has argued that “net tariffs will lower the US trade deficit and thereby boost real GDP growth while slowing the transfer of US assets into foreign

hands, thereby preserving US wealth.” As quoted by Gillian Tett, ‘That is Maganomics’, *The Financial Times*, 4-5 January 2025.

¹⁰ The characterization of Donald Trump’s approach as “zero-sum” is made by David Frum during the podcast “How should Canada understand Trump’s 25% tariffs?” *In Conversation with David Frum* posted on *The Hub Canada*. <https://www.youtube.com/watch?v=7IRJc7sXL8M>

¹¹ For a list of these issues see Congressional Research Service. In Focus. U.S.-Canada Trade Relations. July 8, 2024. <https://crsreports.congress.gov/product/pdf/IF/IF12595>

¹² While the Ontario and BC premiers have stated their support for taxes on exports of energy from their province to the US, the premiers of other energy exporting provinces have publicly voiced their opposition to such retaliation. The Premier of Alberta has been particularly adamant that taxes not be levied on her province’s exports of petroleum to the US. See Steven Chase, Laura Stone and Kelly Cryderman, “Canada weighs export tax to counter Trump tariff pledge,” *The Globe and Mail*, December 13, 2024. Alberta is the largest source of US petroleum exports; they account overwhelming for Canada’s trade surplus with the US: a surplus that Trump points to as evidence that the US is subsidizing Canada through CUSMA.