Vancity Investment Management

Impact of U.S. tariffs on Canada and markets.

Earlier this year, President Donald Trump announced a series of tariffs on its two closest trading partners—Canada and Mexico. Then, on Wednesday, April 2, 2025, he unveiled tariffs on imports from nearly all U.S. trading partners, using the International Economic Powers Act of 1977 to justify the levies, and declaring the U.S.' trade deficit a national emergency.

Impact to Canada.

Under existing guidelines, goods compliant under Canada-United States-Mexico agreement (CUSMA) will continue to be free of tariffs, while non-compliant goods face tariffs of 25 per cent (If this is later axed, it will instead be 12 per cent reciprocal tariffs.) with a 10 per cent carve out for energy and potash. The 25 per cent tariff on steel and aluminum is also still in place. In response to the 25 per cent tariff on autos, Canada announced retaliatory tariffs on US-made vehicles that aren't compliant with CUSMA, and on the non-Canadian content in cars and trucks.

Fixed income market response.

Global bond markets initially observed broad price increases after the Wednesday, April 2, 2025 tariff announcement, with yields declining materially on expectations of negative implications for global economic growth. However, there's since been a meaningful reversal, led by U.S. Treasury yields rising the most over a three-day period since 2008. Market participants have significant concerns regarding the overall inflationary impact of a global trade war and also appear to be challenging the U.S. administration's need for lower interest rates.

While there are still expectations for additional policy easing from the Bank of Canada this year, domestic longer-dated bond yields have also shifted higher through a combination of rising Government of Canada yields and widening credit spreads.

Given the high level of uncertainty within the context of global trade and future economic growth, particularly in Canada, fixed income investments offer attractive yield carry and potential for capital appreciation.

Equity market response.

The equity market reaction has been understandably severe, as the reciprocal tariff announcement was considered by most to be close to a worst-case scenario, with expectations it will increase inflation and push many countries into a recession. Since the announcement, the S&P 500 has seen two of the largest three-day declines in the past 75 years, along with one of the largest one-day increases, which followed the 90-day pause, highlighting just how sensitive the market is to tariff announcements.

Certain industries, such as consumer discretionary, which relies heavily on imports from emerging markets such as China and Vietnam, are being hit the hardest. We do expect countries to negotiate with the U.S. and any further relief in tariffs would be viewed positively by the market. The impact of tariffs is also very much company dependent. While many will feel the impact, others will see minimal to no impact. Although the tariffs are broad-based across countries, the impact is much more specific when it comes to individual industries and companies.

We also want to highlight that while this is a unique situation, the equity markets have faced a number of "unique" situations over time, including most recently, the wars in Ukraine and the Middle East, and the COVID-19 global pandemic which shut down the majority of the world for a significant amount of time. However, through these trials and tribulations, the equity markets have continuously provided a strong compounded return of nine per cent (CAD) per annum over the long-term. Looking back at the past 44 years ending in 2024, the equity markets have been positive in 34 of those years, despite an average intra-year drop of more than 12 per cent each year.

Background on tariffs.

A tariff is essentially a tax imposed by a country on imported goods. The reasons can vary, including as a way to raise revenue, protect domestic industries, or even to exert political leverage over another country. The tariff isn't paid by the exporting country, but rather by the company or consumer importing the goods. For example, the tariffs announced by the U.S. will be paid by U.S. businesses and consumers who are importing the goods. The impact on prices to the end user, in this case the U.S. consumer, will depend on how much of the tariff gets passed on through price increases.

Retaliatory tariffs and the ensuing trade war.

The U.S.' proposed tariff rates, which vary by country, were set to remain in effect until the president determined the threat was "satisfied, resolved, or mitigated." A fact sheet released by the White House on Wednesday April 2, 2025, stated: *the order contains modification authority, allowing President Trump to increase the tariff if trading partners retaliate or decrease the tariffs if they take significant steps to remedy non-reciprocal trade arrangements and align with the United States on economic and national security matters.*

In addition:

- The reciprocal tariffs were set at half of the tariff rates the U.S. said it's being charged by trading partners, with a minimum baseline of 10 per cent.
- The tariffs were scheduled to take effect on Saturday, April 5, 2025, but higher individualized tariff rates were set to be implemented for certain countries on Wednesday, April 9, 2025 including a 34 per cent tariff on China and a 20 per cent levy on the European Union (EU).
- The tariff rates are equal or higher than 20 per cent for the U.S.'s major trading partners—EU (20 per cent), Mexico (25 per cent), China (34 per cent), Canada

(25 per cent on certain goods), and Japan (24 per cent). Note: Canada and Mexico were spared from the reciprocal tariffs announced on Wednesday, April 2, 2025.

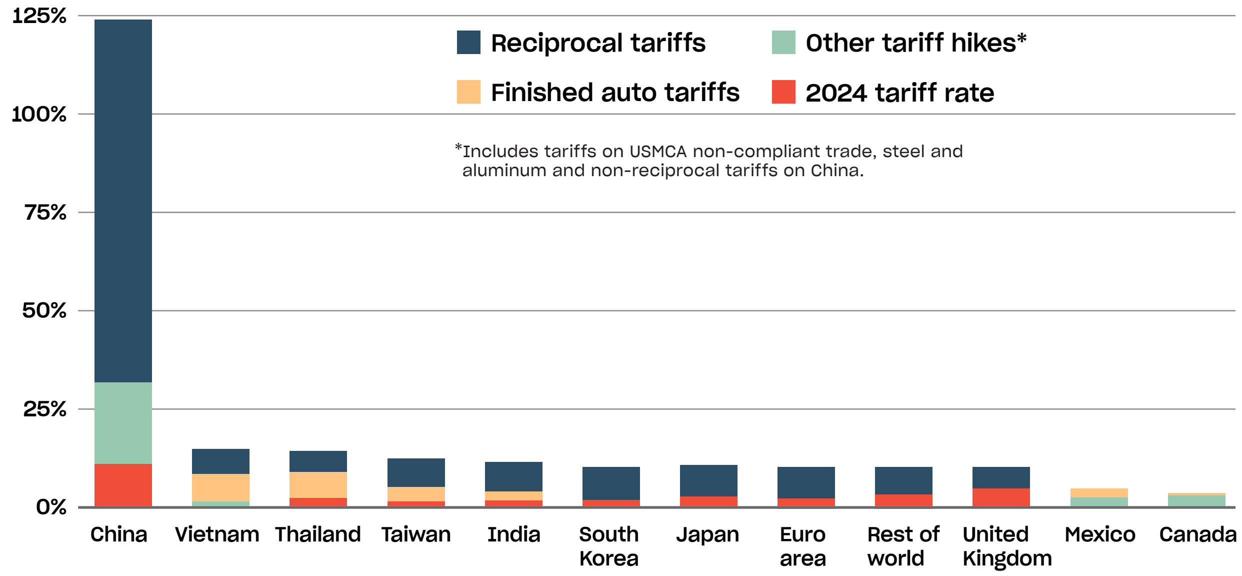
- Countries with the highest reciprocal tariff rates are mostly developing/emerging economies with small U.S. trade shares, including Cambodia (49 per cent), Laos (48 per cent), and Vietnam (46 per cent).
- A new 25 per cent tariff on foreign-produced autos also came into effect. This is on top of the 25 per cent steel and aluminum tariffs in place since Wednesday, March 12, 2025.

In response, certain countries, along with the EU, announced retaliatory tariffs against the U.S., further deepening the trade war. Of particular note, after a series of tit for tat increases, the U.S. and China pushed tariffs levied on one another to 145 and 125 percent respectively.

On Wednesday, April 9, 2025, the U.S. once again changed its stance, creating even more uncertainty and volatility in the stock market. The President announced he was pausing the reciprocal tariffs for 90 days on countries facing rates higher than the 10 per cent baseline (excluding China), after the White House said more than 75 countries had asked to begin trade negotiations.

U.S. import tariff rate by country/region.

Custom duties as percent of imports, ranked by increase in rate 2025 to-date.



Tariff rates are evolving rapidly. This chart was accurate as of April 10, 2025.

Source: U.S. Census Bureau, RBC Economics.

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