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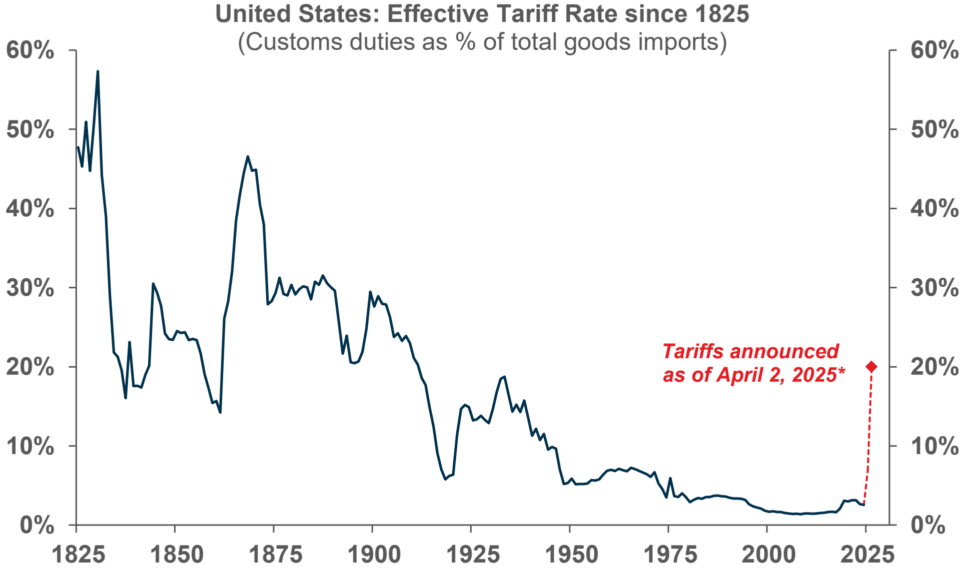
Key charts on our radar

CIO Office

April 3, 2025

U.S. tariffs: 100 years back in time

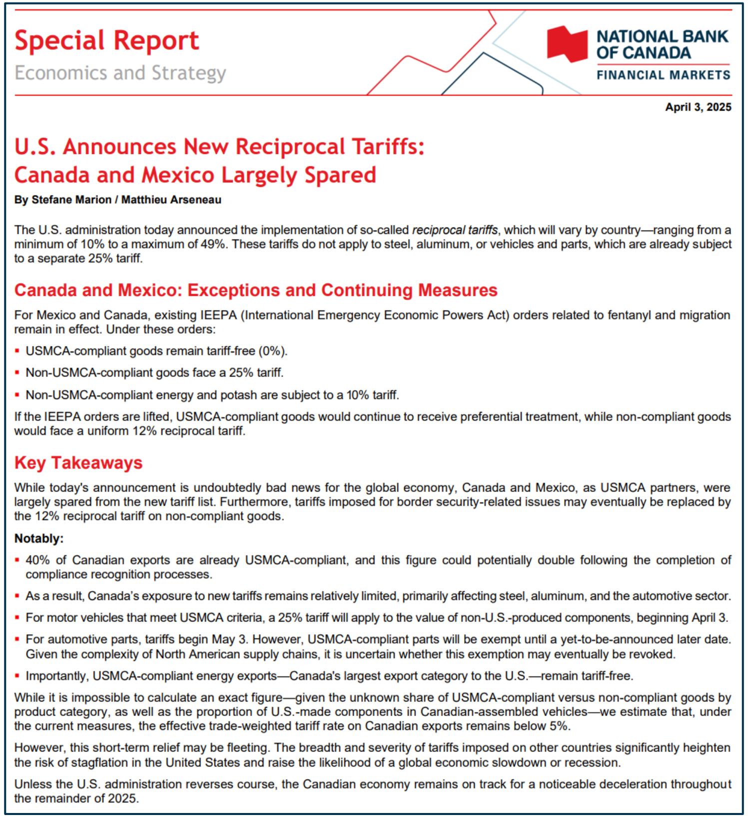
So-called reciprocal tariffs announced on April 2 surprised markets by their magnitude, with an effective tariff rate heading toward 20%. This compares to the highs of the 1930s and represents an increase approximately 12x higher than during the previous trade war, in 2018.



CIO Office (Data via Refinitiv, US Census Bureau). *Estimate from Bank of America.

Canada (relatively) spared this time

At first glance, Canada seems to have been largely spared from the latest reciprocal tariff announcement. According to our economists, although it is impossible to calculate an exact figure, the effective trade-weighted tariff rate on Canadian exports to the U.S. should remain below 5% (for full details, click here). This compares with 54% for China and around 20% for Europe.



Special Report

Economics and Strategy

NATIONAL BANK OF CANADA

FINANCIAL MARKETS

April 3, 2025

U.S. Announces New Reciprocal Tariffs: Canada and Mexico Largely Spared

By Stefane Marion / Matthieu Arseneau

The U.S. administration today announced the implementation of so-called *reciprocal tariffs*, which will vary by country—ranging from a minimum of 10% to a maximum of 49%. These tariffs do not apply to steel, aluminum, or vehicles and parts, which are already subject to a separate 25% tariff.

Canada and Mexico: Exceptions and Continuing Measures

For Mexico and Canada, existing IEEPA (International Emergency Economic Powers Act) orders related to fentanyl and migration remain in effect. Under these orders:

- USMCA-compliant goods remain tariff-free (0%).
- Non-USMCA-compliant goods face a 25% tariff.
- Non-USMCA-compliant energy and potash are subject to a 10% tariff.

If the IEEPA orders are lifted, USMCA-compliant goods would continue to receive preferential treatment, while non-compliant goods would face a uniform 12% reciprocal tariff.

Key Takeaways

While today's announcement is undoubtedly bad news for the global economy, Canada and Mexico, as USMCA partners, were largely spared from the new tariff list. Furthermore, tariffs imposed for border security-related issues may eventually be replaced by the 12% reciprocal tariff on non-compliant goods.

Notably:

- 40% of Canadian exports are already USMCA-compliant, and this figure could potentially double following the completion of compliance recognition processes.
- As a result, Canada's exposure to new tariffs remains relatively limited, primarily affecting steel, aluminum, and the automotive sector.
- For motor vehicles that meet USMCA criteria, a 25% tariff will apply to the value of non-U.S.-produced components, beginning April 3.
- For automotive parts, tariffs begin May 3. However, USMCA-compliant parts will be exempt until a yet-to-be-announced later date. Given the complexity of North American supply chains, it is uncertain whether this exemption may eventually be revoked.
- Importantly, USMCA-compliant energy exports—Canada's largest export category to the U.S.—remain tariff-free.

While it is impossible to calculate an exact figure—given the unknown share of USMCA-compliant versus non-compliant goods by product category, as well as the proportion of U.S.-made components in Canadian-assembled vehicles—we estimate that, under the current measures, the effective trade-weighted tariff rate on Canadian exports remains below 5%.

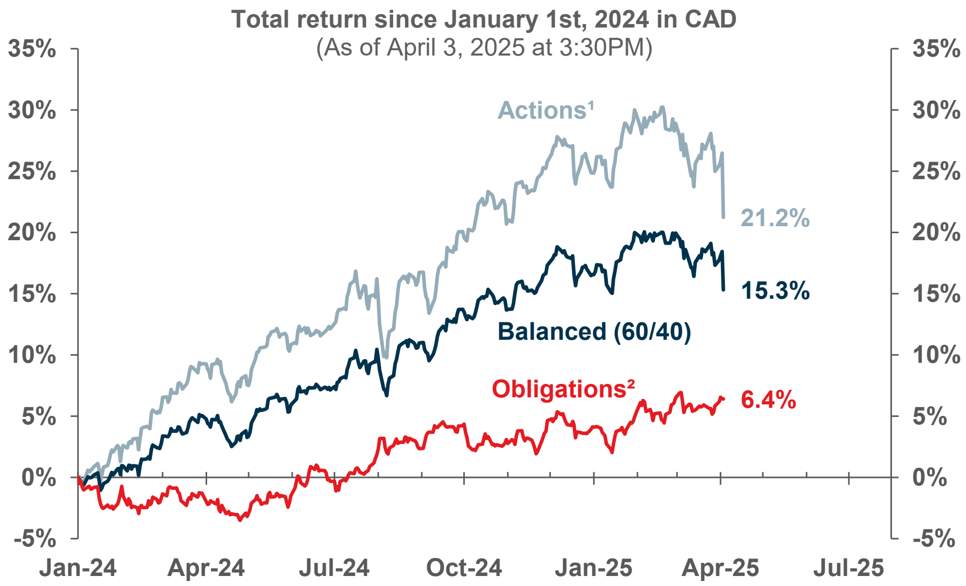
However, this short-term relief may be fleeting. The breadth and severity of tariffs imposed on other countries significantly heighten the risk of stagflation in the United States and raise the likelihood of a global economic slowdown or recession.

Unless the U.S. administration reverses course, the Canadian economy remains on track for a noticeable deceleration throughout the remainder of 2025.

CIO Office (Data via Refinitiv).

Markets reacted strongly...

In the face of the tariff shock, equity markets fell sharply, while Canadian bonds remained relatively stable. Taken together, this brings a typical balanced portfolio back to its January level.



CIO Office (Data via Refinitiv). *35% S&P/TSX, 35% S&P 500, 20% MSCI EAFE, 10% MSCI EM all in CAD.

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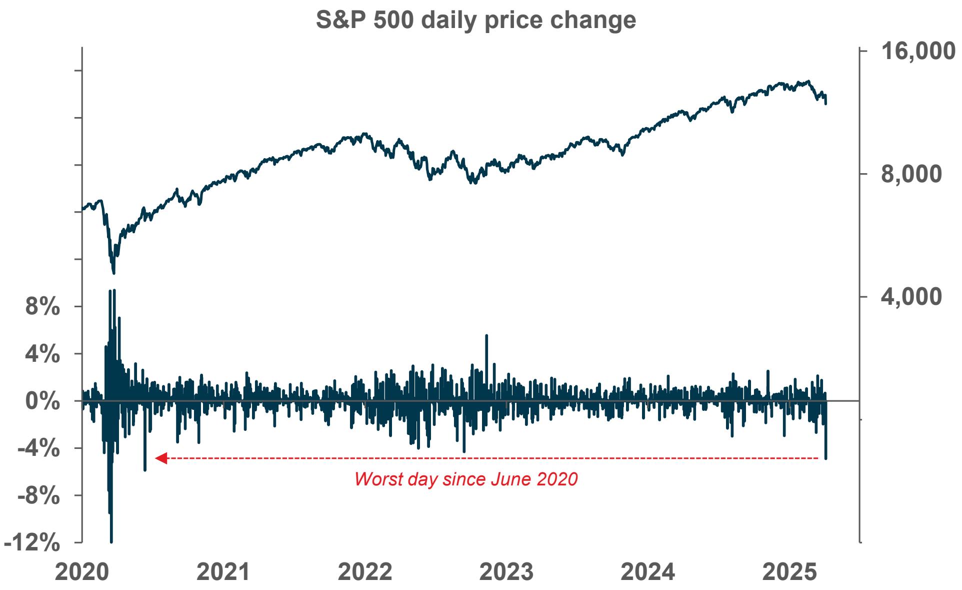
... and the next few days promise to be highly volatile

Within equities, the reaction was particularly strong in the United States. For the S&P 500, it was the worst day since June 11, 2020, taking the index back to its August 2024 levels.



CIO Office (Data via Refinitiv).

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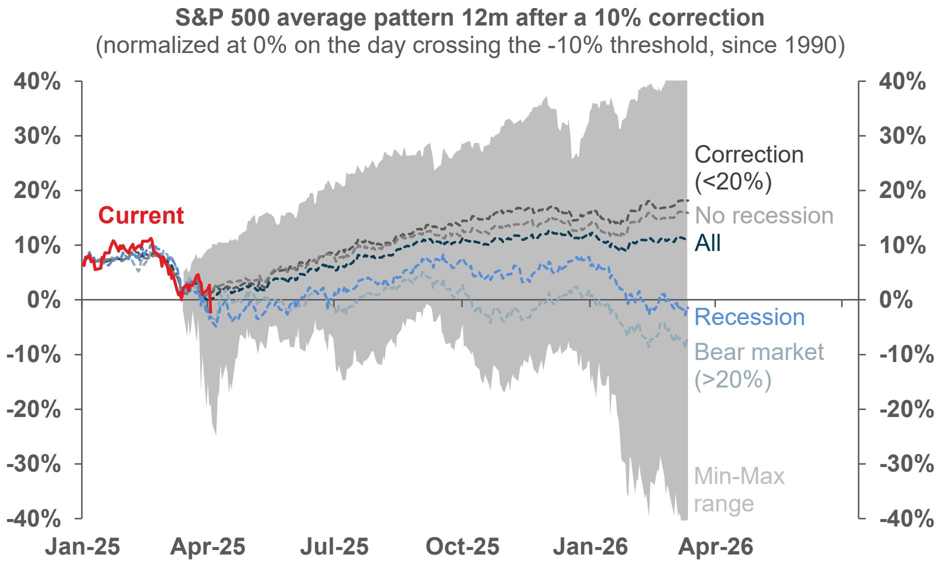
The spectre of recession hangs over the markets...

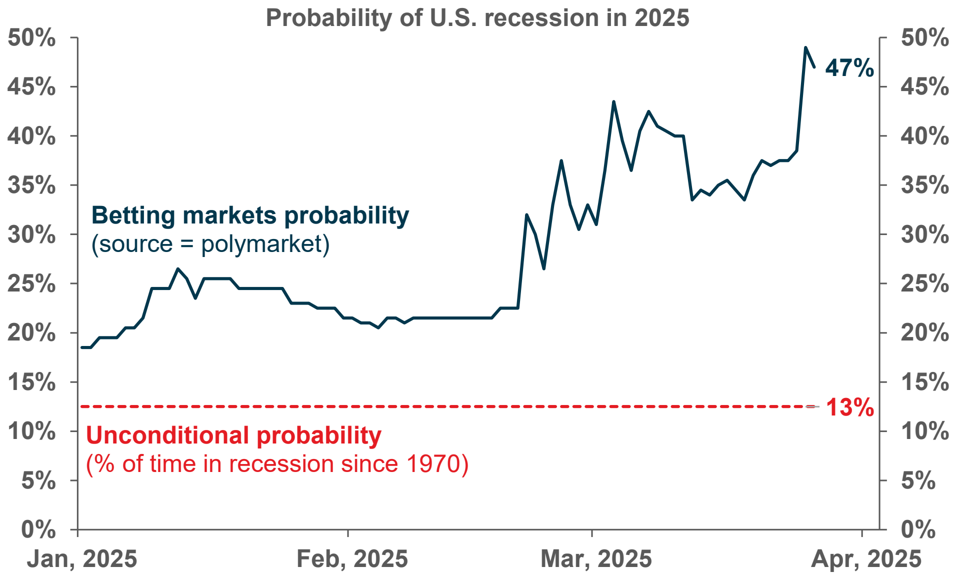
This is not the first equity market correction (pullback of at least 10%), but the 17th since 1990. On average, stocks tend to recover over the following year. However, the current context is anything but conventional, and recession risks are very real.



CIO Office (Data via Refinitiv).

... while probabilities continue to rise

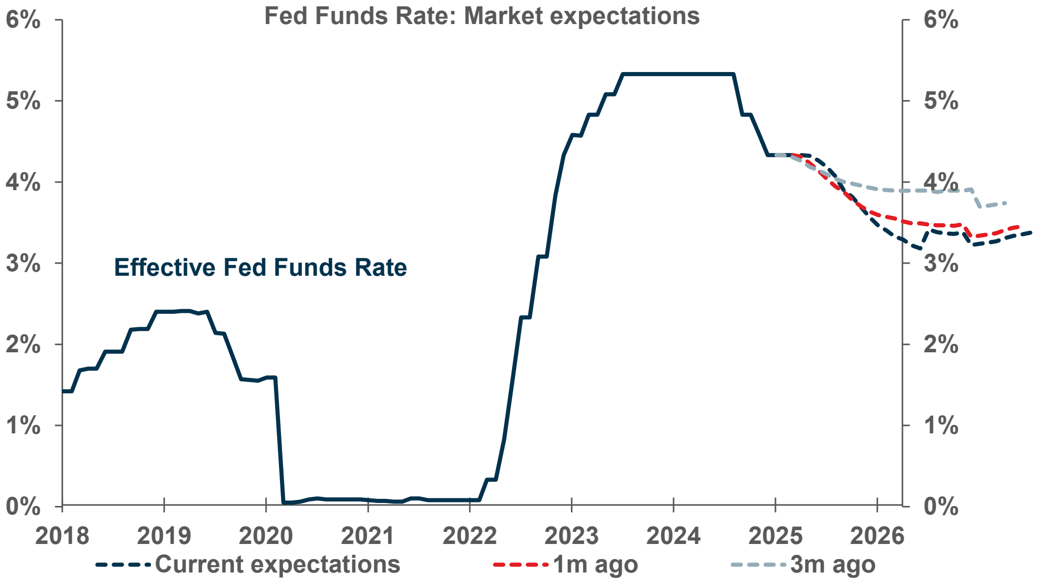
The risk of a recession is never zero. Since 1970, the U.S. economy has been in recession approximately 1 year out of 8. However, the odds of an economic contraction in 2025 are now closer to 50% according to the betting markets, which is not particularly exaggerated if the announced tariffs remain in place for an extended period.



CIO Office (Data via Polymarket). As of April 3, 2:40PM.

Rates are likely to drop further

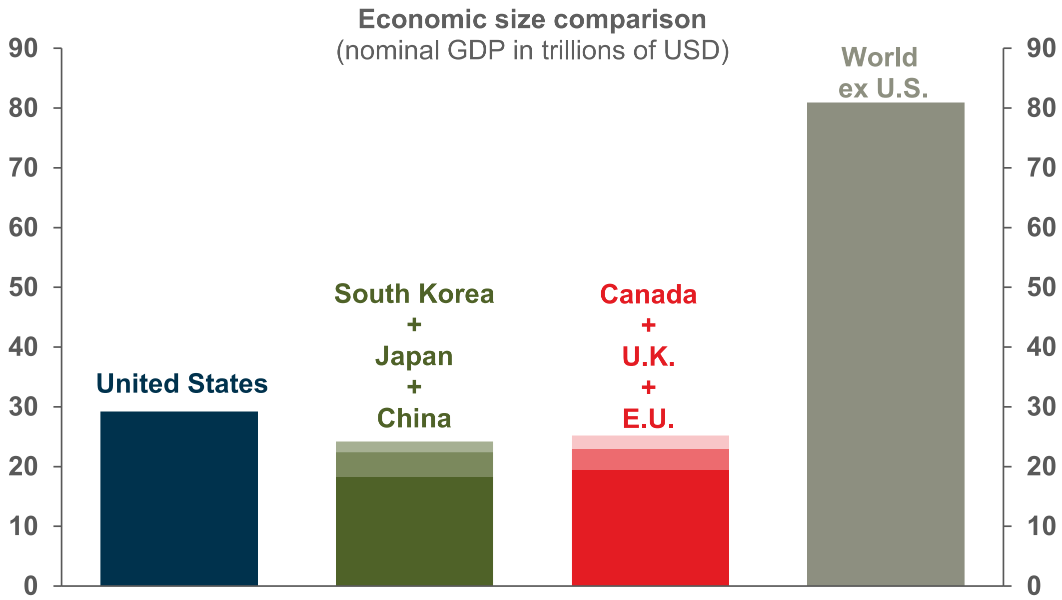
Over the coming weeks, we'll be keeping a close eye on the Federal Reserve's intentions, which, according to market expectations, could cut rates four times over the next year.



CIO Office (Data via Refinitiv).

The U.S. against the world

The big question, however, is how the strategy of retaliation will unfold elsewhere in the world. While the United States seems open to negotiation, its position of strength is not infallible.



CIO Office (Data via Refinitiv, IMF).

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