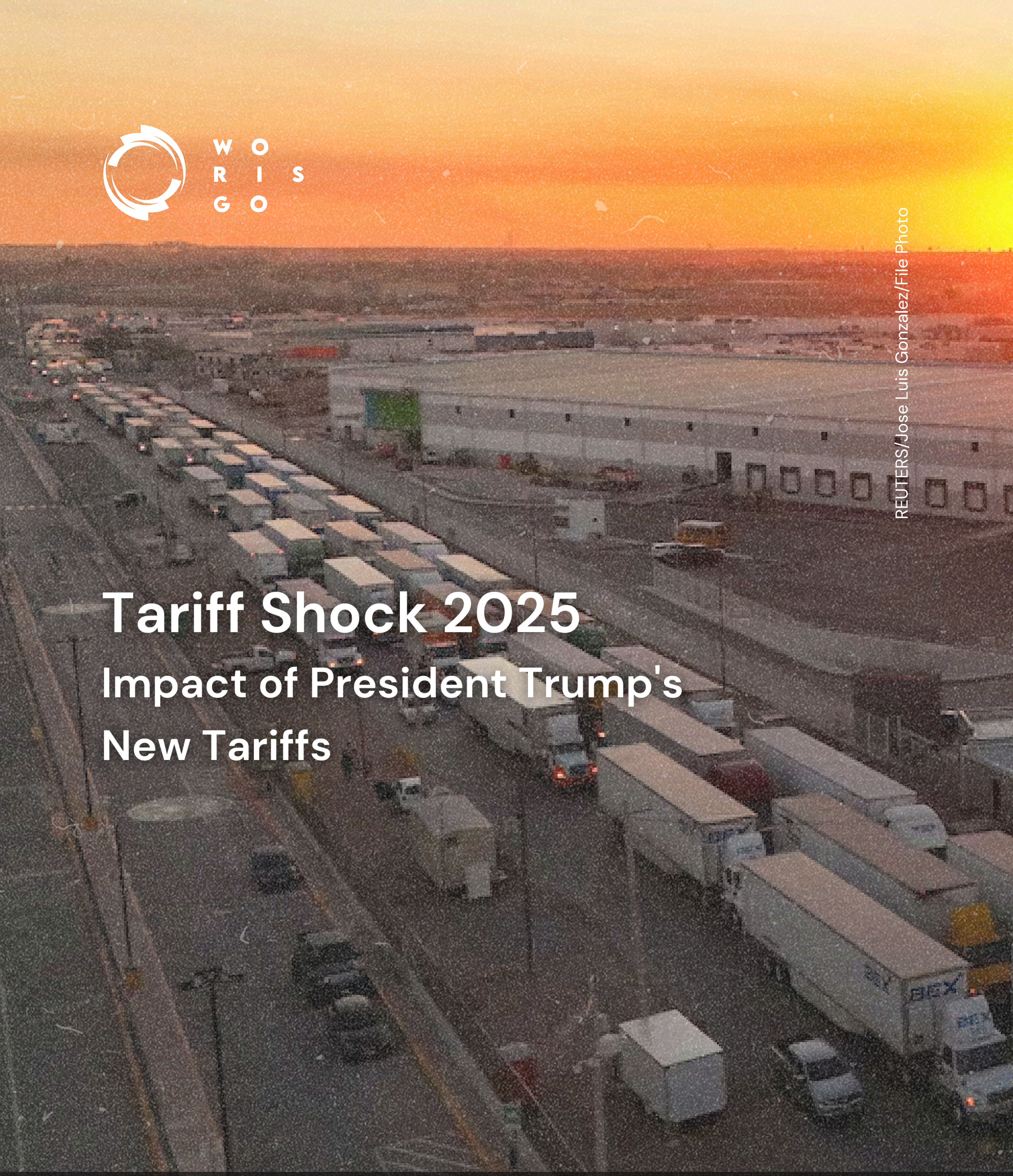

REUTERS/Jose Luis Gonzalez/File Photo

Tariff Shock 2025

Impact of President Trump's New Tariffs

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Executive Summary

President Trump has signed new tariffs on imports from Mexico, Canada and China, marking a sharp escalation in ongoing trade tensions. Effective at 12:01 a.m. ET on Tuesday, the White House justifies the move under the International Emergency Economic Powers Act (IEEPA), declaring an economic emergency tied to drug trafficking—particularly fentanyl, undocumented immigration and large trade deficits. This bypasses lengthy investigations normally required for trade actions, fueling business uncertainty and industry backlash.

Overview of Current Tariff Measures

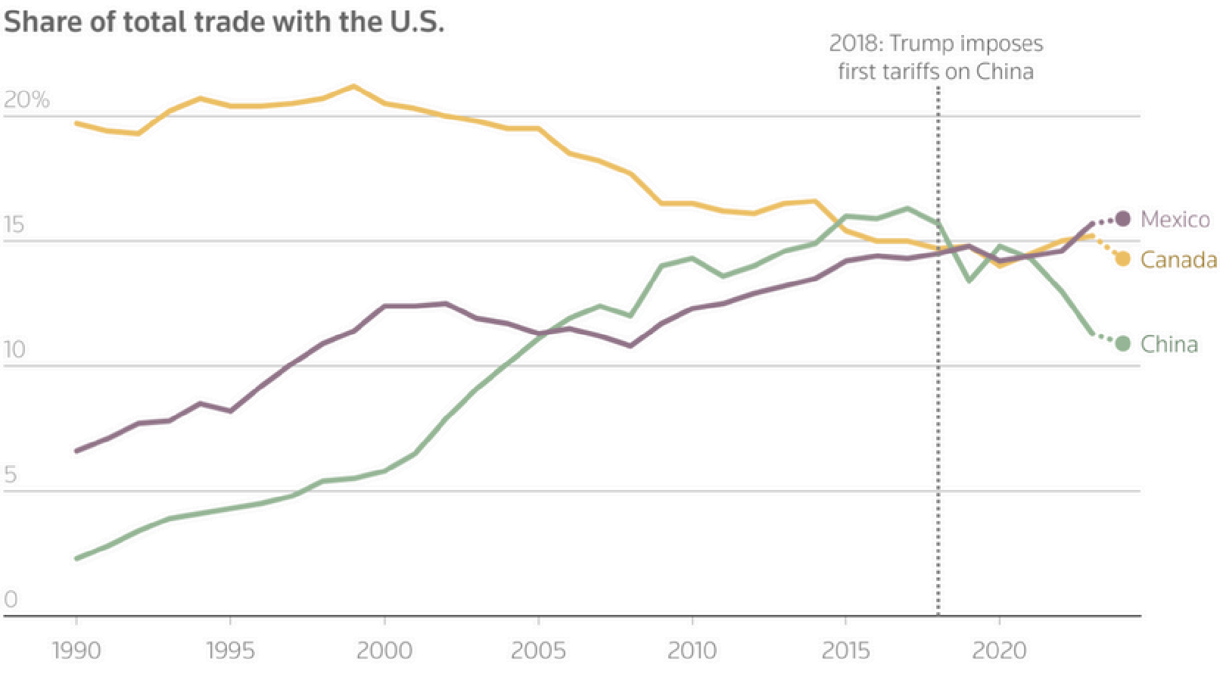
- **Tariffs on Canada (Temporarily suspended for a month):**
  - 25% on nearly all Canadian goods entering the U.S.
  - 10% specifically on Canadian energy exports, including crude oil and natural gas.
- **Tariffs on Mexico (Temporarily suspended for a month)**:
  - 25% blanket tariff on goods from Mexico, spanning automotive goods, electronics and more.
  - If Mexico fails to execute its border security commitments, the tariff will be immediately enforced. The administration is monitoring compliance closely, with trade officials coordinating the next steps.
- **Tariffs on China**:
  - 10% duty on Chinese imports, largely targeting consumer electronics, machinery and intermediate goods.

Background

Global markets are bracing for turbulence after U.S. President Donald Trump launched a trade war with sweeping tariffs on Canada, Mexico and China, threatening to undermine economic growth and reignite inflation. Though tariffs on Mexico and Canada have been temporarily paused for a month, uncertainty remains, leaving U.S.-Mexico-Canada trade in limbo. Trade uncertainties loom as Trump imposes tariffs on three of the U.S.'s largest trade partners.

America's biggest trade partners

Top three trade partners, Mexico, Canada and China, account for about 40% of U.S. trade.



Note: Data is for goods only. Data is annual and through 2023 except 2024 which is through November 2024. Total trade is the sum of exports and imports.

Source: U.S. Census Bureau | Reuters, Feb. 1, 2025 | By Kripa Jayaram

The line charts shows share of total trade of top trade partners of the U.S. i.e. Mexico, Canada and China

Country-by-Country Analysis

Canada

In 2023, Canada shipped over $594 billion worth of goods to the United States, i.e., 77% of its total exports. Oil and gas lead the pack, alone set to face a 10% tariff. That extra charge adds up to $14.3 billion in new costs, straining Canadian producers and U.S. refiners. Meanwhile, Ontario's auto sector—which exported $58 billion in vehicles last year, accounting for 96% of its output—now confronts a 25% tariff that could upend the entire North American supply chain.

Temporary Halt

- Trump agreed to pause tariffs after Canada pledged stronger border security, curbing migration, and tackling fentanyl trafficking. Prime Minister Trudeau committed a $1.3bn plan, including nearly 10,000 frontline workers and appointing a "fentanyl czar." In return, tariffs are suspended for 30 days, giving both countries temporary relief and averting a trade war.

Economic Impact

- Prime Minister Trudeau warns that tariffs may push Canada into a recession, with energy flow disruptions also affecting U.S. refiners. The Canadian dollar has already shown signs of volatility.
- Economic implications will be more significant on Canada's side, but the U.S. will also feel the effects. Ohio could see a $5 billion decline in auto and metal exports to Canada, while Maine may face an impact from tariffs on $320 million worth of lumber and paper exports to Canada.

Canada's Counter-Tariffs Set for Next Month

- Phase 1: $30B in tariffs on U.S. goods, including Orange Juice, peanut butter, alcohol, coffee, appliances, apparel, cosmetics, motorcycles, and pulp & paper.
- Phase 2 (Proposed under consideration): $125B in additional tariffs after a 21-day public comment period. Targets vehicles (incl. EVs), steel, aluminum, aerospace, beef, pork, dairy, trucks, buses, boats, and certain fruits & vegetables.

Mexico

In 2023, two-way trade between Mexico and the United States topped $400–500 billion—built mainly on autos, auto parts, agriculture, and electronics. Now, Mexico faces a 25% tariff on virtually all of its exports to the U.S., a severe blow to the auto sector in particular. As the top auto parts supplier to America, Mexico risks losing revenue and jobs if manufacturers shift production elsewhere to avoid the tariffs.

Temporary Halt

- The 25% tariff on Mexican imports remains active but on hold, pending Mexico's execution of border security measures. If commitments aren't met, enforcement will be immediate.

Potential Retaliation

- Officials hinted at "carousel" tariffs targeting U.S. farm exports, pork, cheese, or processed goods from politically crucial states. Mexico's foreign ministry said it has "Plan A, B, and C" ready, depending on White House actions.

Likely Consequences

- A near 12% drop in the peso is estimated if duties remain. Rising input costs could also affect U.S.-based manufacturers relying on parts from Mexican plants.

Affect on Particular US States and Industries

- Mexico buys 70% of New Mexico's exports, including billions in U.S. semiconductor chips and electrical components—which later return to the U.S. in Mexican-made cars and appliances.
- Texas exports over $20 billion in chips, auto parts, and electrical equipment to Mexico, with southbound trade making up 5% of Texas' GDP.

China

In 2023, China exported around $615 billion worth of goods to the United States—a massive flow now facing a new 10% tariff. While lower than the 25% duties slapped on North American neighbours, even a 10% levy could raise prices on electronics, machinery, and everyday consumer items.

Beijing's Response

- China is challenging the tariffs via the WTO and warning of unspecified "countermeasures." Officials have argued that the fentanyl crisis is a "U.S. problem" that cannot be resolved by taxing all Chinese imports.

Retaliation

- China imposed 15% tariffs on some coal and LNG and 10% on oil, agricultural machinery and vehicles. It also introduced new export controls on metals like tungsten, adding biotech firm Illumina and PVH Group to its "unreliable entities list." Additionally, authorities launched an antitrust probe into Google. Beijing also filed a complaint at the WTO and vowed more action if necessary.

Igniting a Potential Trade War

The U.S. economy will remain largely unaffected by trade barriers, as trade accounts for only a quarter of its GDP. However, Mexico and Canada, which rely on trade for 70% of their GDP, are significantly more vulnerable. More than 80% of Mexico's exports, including fresh produce, automobile parts, and medical equipment, are destined for the U.S. Blanket tariffs could reduce global GDP by 1.4% over two years, according to Gregory Daco, Chief Economist at EY. Mexico's real GDP is projected to decline by 1.6% in 2025 and 4.5% in 2026, as trade with the U.S. constitutes 40% of its GDP. Canada's economy is expected to shrink by 2.7% in 2025 and 4.3% in 2026 due to its high reliance on U.S. trade. Additionally, U.S. inflation may rise, as tariffs increase import costs.

President Trump's escalating trade dispute poses a tremendous risk to interconnected supply chains. Although tariffs on Canada and Mexico have been suspended for 30 days, the 10% duties on Chinese imports remain, and Beijing has retaliated. This tit-for-tat can spiral if neither side backs down, heightening market anxiety and harming overall economic confidence.

Many products cross borders multiple times during manufacturing, and higher duties raise costs at each step, slowing production and reducing investments. The U.S. auto industry, employing around 4 million people, could see vehicle prices rise by up to $10,000, as parts often cross borders 5-7 times before final assembly. U.S. businesses that depend on global supply chains could struggle to maintain competitiveness, while retaliatory tariffs threaten the U.S. export market.

Heightened tariffs and uncertainties in trade policy may also cause companies to delay or redirect projects to other regions, disrupting employment and raising consumer prices. Whether further dialogue can halt a deepening standoff remains uncertain, though negotiations could provide relief if both sides address issues like intellectual property, supply chain security, and fair market access. These actions will be closely watched due to America's key role in global commerce.

WORLD RISK & GOVERNANCE

Sector-by-Sector Analysis

Automotive & Auto Parts

For decades, U.S., Canadian, and Mexican factories have functioned like one giant production line. In 2023 alone, the U.S. imported nearly $69 billion worth of cars and light trucks from Mexico—more than from any other country—and $37 billion from Canada. Auto parts followed a similar cross-border flow, including $78 billion from Mexico and $20 billion from Canada. With a 25% tariff, industry analysts estimate average U.S. car prices could jump by $3,000, putting vehicles further out of reach for consumers already facing a $50,000 average on new cars.

Agriculture & Food

American shoppers rely heavily on Canada and Mexico for produce. In 2023, the U.S. imported $45 billion of agricultural goods from Mexico—63% of all imported vegetables, 47% of fruits and nuts—and another $40 billion in farm products from Canada. A 25% tariff means items like avocados (especially with the Super Bowl looming), tomatoes and cheese could see marked price hikes. Farmers in states that backed Trump also worry about retaliatory tariffs hitting their corn, soybeans, pork and dairy exports—reminiscent of the first Trump administration, when China targeted rural products in a tit-for-tat response.

Energy

Although Canadian oil and gas face “only” a 10% tariff, America depends on heavier Canadian crude that many Midwestern refineries are specifically designed to process. Analysts at TD Economics warn that tariffs on Canadian energy could boost U.S. gas prices by 30 to 70 cents per gallon. Any further expansion of tariffs on Mexico’s energy exports would tighten the squeeze, fueling higher transportation and logistics costs nationwide.

Spirits & Beverages

Tequila and mezcal from Mexico—and whisky from Canada—are already more expensive to import. In 2023, the U.S. purchased $4.6 billion worth of tequila plus $108 million of mezcal from Mexico, and $537 million worth of Canadian spirits. Industry leaders warn that targeting signature products—like tequila, which can only be made in Mexico, or Canadian whisky—will raise prices at bars and restaurants, hurting America's hospitality sector as it struggles to rebound from prior economic setbacks.

Consumer Goods & Electronics

China may face a somewhat lower 10% tariff, but consumer electronics, appliances, and industrial components are still in the crosshairs. Because U.S. importers typically pass costs to shoppers, everything from smartphones to washing machines could see price jumps. Even a small increase can cascade when added to supply-chain disruptions, driving inflation higher.

Risk Assessment

Probability
High
High
Impact

Cross-Border Supply Chain Disruptions

- Suppose a 25% tariff on Canadian and Mexican goods resumes after the month of suspension, coupled with a 10% levy on Chinese imports. In that case, it increases the likelihood of delays and bottlenecks in vital supply chains. Companies that source components (e.g., automotive parts, consumer electronics) from these markets may struggle to maintain production schedules.
- Immediate slowdowns are anticipated at land border crossings, particularly on the U.S.-Canada corridor (notably in automotive manufacturing centres) and along the U.S.-Mexico routes that handle agricultural and electronics shipments.
- Uncertainty over retaliatory measures can lead to last-minute route changes, translating into higher freight costs, potential shortages, and increased lead times for U.S. businesses.

Probability
High
High
Impact

Domestic Price Inflation and Consumer Backlash

- Multiple analyst estimates suggest tariffs on North America and China could add up to 0.7% to core inflation in the U.S., which is an immediate concern for sectors reliant on imported raw materials (e.g., steel, aluminium and electronics components).
- Retailers face pressure to pass on tariff-related costs to consumers. This may reduce purchasing power, particularly in lower-income households.
- Tariffs on Canada, Mexico and China could cost the average U.S. household $1,200 annually, directly reducing consumer spending.

Probability

High

High

Impact

Geopolitical and Diplomatic Fallout

- Rising tariff disputes are straining U.S. trade ties with Canada and Mexico, putting the United States-Mexico-Canada Agreement (USMCA) at risk.
- China has retaliated by launching an antitrust investigation into Google and imposing 15% tariffs on U.S. coal, liquefied natural gas (LNG) and 10% tariffs on U.S. oil and agricultural equipment. A prolonged conflict could create deep mistrust and limit cooperation.
- Ongoing tensions could weaken global partnerships on climate change, security and trade if other countries see the U.S. as unreliable.

Probability

High

High

Impact

Risk of a Broader Global Trade War

- Trump's threats to impose tariffs on the EU for perceived trade imbalances could provoke retaliatory measures from the world's largest customs union.
- If the US imposes 25% tariffs on cars from Japan, Germany, and Korea, global auto markets will be adversely affected, leading to shifts in demand and retaliatory actions from impacted nations.
- India and Vietnam benefited from previous US-China trade shifts; however, prolonged uncertainty could disrupt emerging economies by making trade policies unpredictable.

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