## ECONOMIC VIEWPOINT

# The Trade Conflict Between Canada and the United States Is Intensifying

The failure of trade negotiations between Canada and the United States has resulted in the imposition of 50% tariffs on products representing approximately 5% of Canadian exports to the United States that had previously been exempt under CUSMA. Canadian retaliatory tariffs ranging from 15% to 50%, depending on the product category, on nearly C$28B of imports from the United States will also add pressure to our economy as of September 8, 2026, by reducing consumers' purchasing power, squeezing some corporate profit margins and boosting inflation. As a result, Canada's average effective tariff rate on imports from the United States could rise from 2.8% to 6.4%.

### Canada: Lower Growth and Increased Inflation Ahead

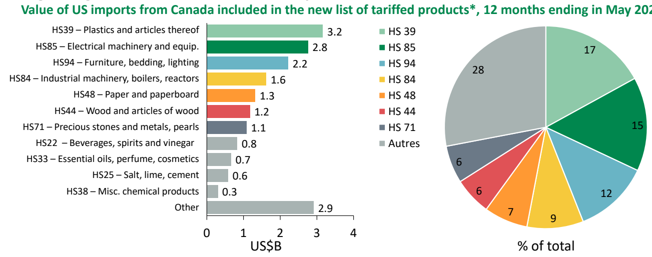
The combined result of this escalation in trade tension with the US will be slower real GDP and employment growth along with increased inflation. But we don't expect these measures will lead to a recession in Canada. If the tariffs are kept in place on both sides of the border, real GDP growth could slow by 0.2 percentage points (ppts) to 0.6% and 0.4 ppts to 1.7% in 2026 and 2027, respectively. The unemployment rate could reach 7% by the end of the year, up from 6.4% in July. Meanwhile, inflation next year could be 0.2 to 0.3 ppts higher than it would be otherwise. This would make the difficult position the Bank of Canada has found itself in since March 2026—needing to balance higher inflation and weaker growth—even more challenging. However, at this moment, we have maintained the view that the Bank of Canada is likely to raise the policy rate by 50 basis points in the first half of 2027, as published in our August 2026 Economic and Financial Outlook. These economic impact estimates also don't account for the increased supports for affected businesses and workers announced by the federal government which, at $7.5B, should be broadly offset by additional tariff revenues. That said, the risks to the Canadian economy remain to the downside, due to a possible further escalation in trade tensions between Canada and the US.

### Quebec: The Hardest-Hit Province and Among Those with the Least Room to Manoeuvre

The impact of the new US measures is expected to be greater in Quebec than in most other provinces because of the high degree of integration between its manufacturing sector and the US market, particularly for products subject to sector-specific tariffs. The United States remains the destination for nearly 70% of Quebec's merchandise exports. However, its share fell from 73.3% in 2024 to 69.7% in 2025, as exports to the United States declined by 7.2% while those to the rest of the world rose by 11.0%. This shift nevertheless remains insufficient to materially reduce Quebec's exposure to the new US trade measures.

Although aerospace and certain minerals remain largely protected, several sectors already weakened by sector-specific tariffs continue to face significant pressure (graph 1). Quebec exports of primary aluminum to the United States fell by 22% between the first half of 2024 and the first half of 2026, while exports of non-ferrous metals dropped by 55%. Lumber (-34%) and light trucks (-55%) also posted sharp declines. In some cases, such as aluminum, companies have managed to partially diversify their export markets. However, these new markets offset only

**Graph 1**
**The New Potential Tariffs Target Machinery, Plastics, Furniture and Lighting Fixtures, Wood and Paper Products**
Value of US imports from Canada included in the new list of tariffed products*, 12 months ending in May 2026




* Tariffs of 50% (since August 22).
United States International Trade Commission, The White House, and Desjardins Economic Studies

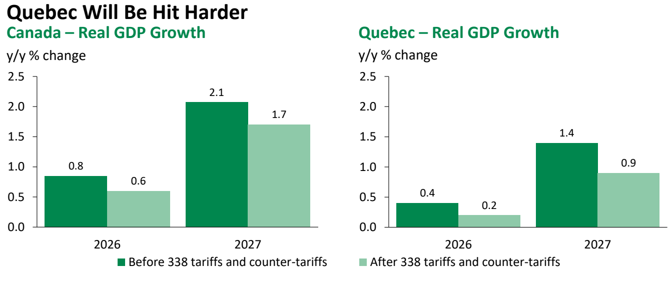
Jimmy Jean, Vice-President, Chief Economist and Strategist • Randall Bartlett, Deputy Chief Economist • Francis Généreux, Lead Economist
Laura Gu, Senior Economist • Florence Jean-Jacobs, Principal Economist • Sonny Scarfone, Principal Economist • LJ Valencia, Economist
Desjardins Economic Studies: 514-281-2336 or 1-866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • desjardins.com/economics

part of the losses incurred in the United States, and such a shift remains more difficult in several other sectors.

The main change is the broader scope of the tariffs. Whereas approximately 17% of Quebec exports to the United States were subject to one tariff or another before April 2026, that share would now exceed one-quarter. Since August 22, roughly C$8B in additional exports have been targeted—more than 9% of Quebec exports to the United States—including plastics, paper and paperboard products, cement, furniture and lighting fixtures, textiles, cosmetics, certain equipment and other manufactured goods that had previously benefited from CUSMA protection. The shock is therefore spreading to a larger number of SMEs and value-added sectors, in addition to generating spillover effects for trade-dependent industries such as transportation and warehousing and wholesale trade.

These measures come at a time when Quebec's growth outlook was already constrained by population aging and weak productivity gains. In particular, Quebec lags several comparable jurisdictions in investment per worker, making it more difficult to catch up in ways that would support productivity gains and business competitiveness. By reducing predictability for exporters, the escalation in trade tensions risks further dampening the investment that would be needed to strengthen the economy's growth potential. Consequently, we have revised down our real GDP growth forecasts for 2026 and 2027, from 0.4% to 0.2% and from 1.4% to 0.9%, respectively (graph 2). The labour market is also expected to weaken further, with the unemployment rate projected to hover around 6% until the end of 2027. The main risk is therefore not so much a tariff-induced recession as persistently weaker growth in an economy already facing significant structural challenges.

**Graph 2**
**The Tariff Adjustment Is Manageable at the Canadian Level; Quebec Will Be Hit Harder**

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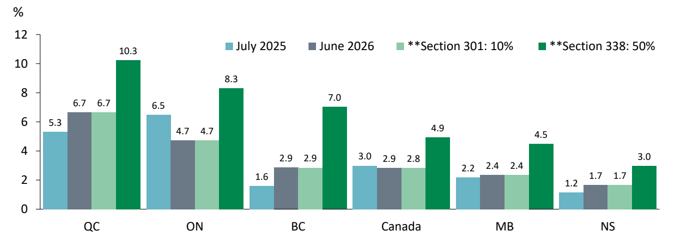
## Other Provinces: A Wider Regional Divide

The latest round tariffs will further exacerbate economic divergences across the provinces. While earlier US tariffs fell most heavily on Quebec and Ontario through their exposure to the auto and metals sectors, the latest measures disproportionately affect BC through targeted plywood and other value-added wood products. As a result, the effective tariff rate on BC exports to the US has risen from the middle of the provincial pack to nearly the same level as those of Quebec and Ontario (graph 3). At the same time, if retaliatory tariffs are implemented as planned on September 8, the average duties faced by BC importers could more than quadruple, from 1.0% to 4.3%, the second-highest rate among the provinces.

**Graph 3**
**Quebec, Ontario and BC Are Seeing the Sharpest Increase in Tariffs Faced**

Average effective US tariff rates on imports from Canada, by province (not seasonally adjusted)*

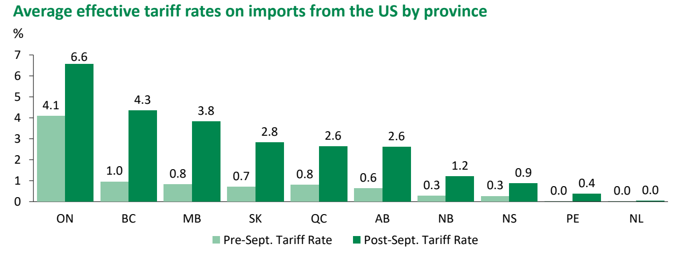



* Average effective tariff rate based on duties calculated at the HS6 level and weighted by provincial exports to the United States. These data include broad-based tariffs (IEEPA, Section 122) and sectoral tariffs (Section 232) but exclude countervailing and anti-dumping duties on softwood lumber.** Desjardins estimate based on customs data as of June 1, 2026. Section 301 reflects the new broad-based tariff, while Section 338 reflects the proposed 50% tariff threat, combined with the new broad-based tariff.
Statistics Canada, U.S. International Trade Commission and Desjardins Economic Studies

Ontario remains among the provinces most exposed to escalating US-Canada tensions. With roughly 10% of its exports directly affected by the latest round of US tariffs, the province's effective tariff rate on exports to the US could nearly double to over 8%. The impact is spread across a broad range of manufactured products, including electrical machinery and equipment, industrial machinery, plastic packaging, lighting fixtures, and precious stones and metals. The tariffs add further downside risk to an already subdued provincial outlook as weak trade and business investment pushed Ontario's economy into two consecutive quarters of contractions in late 2025 and early 2026. Add to this the province's heightened exposure to stagflationary impacts of the proposed retaliatory tariffs (graph 4), and we expect the economy to record virtually no real growth in 2026, followed by a modest rebound of 1.5% in 2027.

**Graph 4**
**Ontario Will Continue to be Subject to the Higher Tariffs on Imports from the US**

Average effective tariff rates on imports from the US by province




Government of Canada, Statistics Canada and Desjardins Economic Studies

Manitoba and Nova Scotia are also affected by the latest US import tariffs, though to a lesser extent, with approximately 5% of each province's exports covered by the measures. Elsewhere, the impact should be relatively limited, with effective tariff rates expected to remain below 1% in Alberta, New Brunswick, Newfoundland and Labrador, and Saskatchewan. These provinces should therefore remain insulated from the direct effects of tariffs, leaving their growth outlooks largely unaffected. However, they are less immune to the impact of the retaliatory tariffs, with the average effective tariff rate on Manitoba's imports rivalling BC's while importers in Saskatchewan and Alberta could face rates comparable to Quebec's. The Atlantic provinces, meanwhile, remain less exposed on the import side.

### United States: Very Limited Effects

As for the US economy, the new tariffs on imports from Canada are not expected to have a significant impact on real GDP growth or the labour market. According to our estimates based on 2024 trade flows, the theoretical effective US tariff rate would rise only slightly—by approximately two-tenths of a percentage point. Moreover, for products targeted by the new tariffs, imports from Canada account for a small share compared with imports from the rest of the world. Indeed, of the US$266.0B in targeted goods imported by the United States from January to June 2026, only US$11.0B came from Canada, or approximately 4.1% of the total. It may therefore be relatively easy for US importers to turn to other foreign suppliers. The measure is also too modest to have a perceptible influence on US consumer price trends. The same conclusion applies to the impact of Canada's reciprocal measures on US exports. Tariffs affecting approximately US$20B in US-made goods will not materially alter the outlook for a US economy of nearly US$32T. That said, the effects could be more noticeable in certain sectors or regions. Nor should the political issue be underestimated: with the midterm elections about two months away, launching a new trade offensive is difficult to reconcile with voters' main concern—an easing of cost-of-living pressures.

### Government Support Measures: Amid the Immediate Urgency, the Need to Adapt Must Not Be Overlooked

In response to the 50% tariffs imposed under Section 338, governments announced several support measures (table 1). Ottawa introduced a C$7.5B package combining liquidity support for businesses, assistance for workers, and measures to promote adaptation and investment. The Quebec government launched the FORCE program (Offensive Fund to Strengthen Economic Capacity), administered by Investissement Québec, as well as a new tariff-related stream under the PAUPME emergency assistance program for small and medium-sized businesses, delivered by regional county municipalities. Ontario, for its part, expanded eligibility for its Protect Ontario Financing Program (table 2 on page 4).

## Table 1
### Measures announced by the federal government

| Measure | Type | Target | Eligibility (main criteria) | Duration / Maturity |
|---|---|---|---|---|
| **Regional Tariff Response Initiative (+$1.5 billion; $3.45 billion total)** | Grant — non-repayable contribution of up to $3M, including $2M for cash flow; Repayable contributions also available | SMEs, all sectors; steel stream | Demonstrated tariff exposure; proposed adaptation or liquidity needs; Evaluation by the Regional Development Agencies | Envelope over 4 years; Enhancement effective September 2026 |
| **BDC — Pivot to Grow, new liquidity component ($500M)** | Loan | SMEs (revenue threshold lowered to $1M) | Directly affected businesses, all sectors; loans of $250K to $5M | 0% interest for the first 12 months; interest only for 36 months; Amortization over 96 months |
| **Canada Strong Diversification Fund ($2 billion)** | Contributions — repayable / non-repayable split not disclosed | Affected businesses, including medium-sized | Shovel-ready projects, including capital asset maintenance; expedited intake | Not specified |
| **Rapid Supports for Workers and Employers ($3.5 billion)** | Employment Insurance transfers and income supplement (replacement rate increased from 55% to approximately 70%) and training grant of up to $1,000 per participant | Workers and employers | Termination of employment; for Work-Sharing, verifiable reduction in activity and employee agreement | Unemployment insurance extension varying between 8 and 12 months |
| **Large Enterprise Tariff Loan — CEEFC ($10 billion)** | Loan, with warrants up to 20% of the voting rights (public companies) | Large companies (revenues of approximately $150M and above) | Market funding previously exhausted; no insolvency filing; solvency as at Dec. 31, 2024; Floor rate: 10-year GoC bond + 25 bps | 36-month coverage; Term up to 15 years |

Government of Canada and Desjardins, Economic Studies

## Table 2

### Measures announced by the governments of Quebec and Ontario

**Quebec**

| Measure | Type | Target | Eligibility (main criteria) | Duration / Maturity |
|---|---|---|---|---|
| FORCE (Investissement Québec) | Loan up to $50M, interest-free in the 1st year and then a stepped rate | Medium and large companies (turnover ≥ $2M) | Manufacturing or primary sector; U.S. tariff≥ 25% since March 4, 2025; Registered in Quebec and in business for at least 2 years; profitability in one of the last two financial years; over $10M, strategic company status recognized by the MEIE | Until March 31, 2028; 7-year term, 24-month principal reimbursement moratorium |
| PAUPME — US tariff stream (RCMs) | Loan of up to $150K, at 0% with a 12-month principal moratorium | Small businesses ($1 to $2M in revenue) | At least 25% of 2024 revenue derived directly or indirectly from exports to the US; a decline in turnover of at least 20% compared to 2024; head office in Quebec and registered with the REQ for at least 2 years; up to 75% of the 12-month liquidity requirement | Terms and conditions in effect until March 31, 2028 |

**Ontario**

| Measure | Type | Target | Eligibility (main criteria) | Duration / Maturity |
|---|---|---|---|---|
| Protect Ontario Financing Program ($1 billion, expanded eligibility) | Term loan, minimum $250K, rates up to prime | Small and medium-sized enterprises | Sectors covered by Articles 232 and 338; Revenue≥ $2M; at least 10 full-time employees; at least 3 years of operation; federal remedies previously exhausted; Security required | Term up to 72 months; Principal reimbursement holiday of up to 12 months |
| Ontario Together Trade Fund ($150M), Trade-Impacted Communities Program ($40M), Manufacturing Investment Tax Credit | Grants and tax credits | SMEs and communities | Market diversification and supply chain strengthening projects | In progress; tax credit valued at $2.7 billion over 5 years |

Governments of Quebec and Ontario and Desjardins, Economic Studies

Common principles across these programs include meeting working-capital needs, imposing eligibility criteria tied to exposure to US tariffs, and favouring loan instruments over grants. However, these measures are not new. For example, PAUPME, like the Canada Enterprise Emergency Funding Corporation, which administers the federal loan program for large businesses, is a vehicle inherited from the pandemic. Quebec's FORCE program succeeds the FRONTIÈRE program, which expired last March. It is mainly the parameters that are changing: for example, eligible revenue thresholds are being lowered, loan caps are being raised and maturities are being extended.

Overall, these initiatives address immediate liquidity pressures and could help prevent otherwise viable businesses from closing because of cash shortages. However, three shortcomings should be highlighted. First, the viability tests used to determine eligibility appear backward-looking even though the shock is reshaping the outlook. For example, FORCE requires profitability in one of the previous two fiscal years. Yet after 18 months of tariffs, past profitability measured today is a less reliable gauge of a company's future viability in a permanently transformed trading environment.

Second, the parameters are being extended. The federal loan can now cover up to 36 months of liquidity needs, compared with 24 months previously, and can be repaid over 15 years rather than 10. This extension implicitly reflects a change in diagnosis: governments are preparing for a more persistent shock. Yet a significant share of the measures remains designed around a liquidity and bridge-financing approach. Ottawa is devoting only a small portion of its intervention to diversification and investment, notably through a new C$2B fund. This may prove insufficient because the longer the shock persists, the more the economic challenge becomes one of facilitating adaptation through market diversification, supply-chain reorganization and investment, while supporting worker transitions where certain activities are no longer viable.

Finally, coordination among levels of government remains uneven. FORCE describes itself as complementary to federal measures without explaining how that complementarity works. Ontario takes a more explicit approach: businesses must first have exhausted federal remedies—or encountered significant barriers to accessing them—before they can qualify. It thus positions itself as a residual lender for cases that remain in difficulty.

In short, governments face a difficult balancing act. Preventing a sudden and disorderly deterioration of the industrial base is necessary in the short term, but support must also be designed to give businesses time to adapt rather than merely postpone that adaptation. Public finances are no longer what they were in 2020.