Market View
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The levy lowdown: A lot of bark, how much bite?

By Ethan Currie

The tariff-induced roller coaster ride continues, following a ~2 week 'steady state' which began with China/U.S. trade deal progress. With recent developments (and no shortage of Truth Social posts), it is perhaps a natural time to update our assessment of U.S. tariff impacts, as fresh (April) **trade data** were also released this morning. In this *Market View*, we explore current White House tariff policies with a view to legal implications, realized vs unrealized customs revenue, Canada's exposure, and what this all might mean for central bankers on either side of the border.

On May 29th, the U.S. Court of International Trade ruled that President Trump had overstepped his authority by imposing tariffs under the International Emergency Economic Powers Act (IEEPA). That ruling, which has since been paused (on appeal), would deem inappropriate the 'reciprocal' levies, such as border security / fentanyl-related rates. This ruling would not, however, affect existing product- or sector-specific tariffs on U.S. imports, such as those applied to steel, aluminum, and autos, which are imposed legally under Section 232 and 301. In contrast to 'sweeping tariffs', the sector-specific levies seem to be the knee-jerk reaction to the legal dispute, as the import tax on steel and aluminum products was doubled to 50% (effective yesterday). This brings the U.S. average effective tariff rate (AETR) back up slightly, to just shy of 15% (call that half of where 'Liberation Day' tariffs would have suggested). Though the court ruling was a setback for the White House, it's clear there are legal options allowing the President to impose tariffs. While the administration likely hoped they'd have hashed out a number of trade 'deals' by this juncture, negotiations have seemingly been more challenging, as only the **U.K.** has an agreement in-hand. The trade war is far from over.

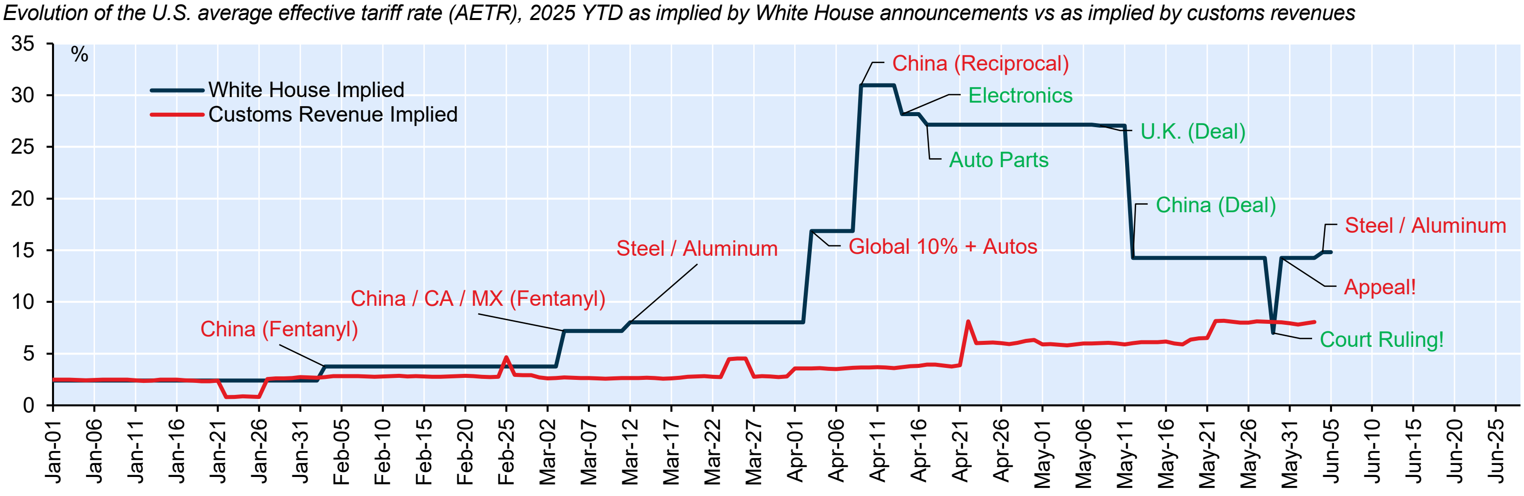
Now, there's been a lot of tariff 'bark' from the White house, but just how much tariff 'bite' has really occurred? There remains a large gap between an AETR estimated using policy announcements relative to one calculated via customs revenues (Chart 1). This discrepancy could capture a number of variables, including implementation and revenue collection lags (importers tend to lump-sum their payments in the second half of each month), a shift in trade behaviour, and / or seasonality in sector-specific trade. While we would expect these two estimates to converge, customs revenue will not get to the levels implied by early-April tariff announcements. Still, we've seen the first batch of 'Liberation Day' revenues captured in the data recently (Chart 2) and it's a non-trivial jump. If sustained, the current tariff regime could be sufficient to 'fund' Trump's '**One, Big, Beautiful Bill**' (Chart 3). Of course, the more trade 'deals' that arrive, and the more levies that are unwound, the lower the scope for tariff revenue.

Like many other nations, Canada hopes to get off the tariff-targeted naughty list. According to PM Carney, "intensive discussions" are taking place, which means an immediate response to the U.S.'s doubling of steel and aluminum tariffs might not be required. As it stands, USMCA compliance remains the largest source of tariff relief (Chart 4), and while today's data reveals still-growing compliance rates (Chart 5), there should be more room to run, ultimately reducing the effective levy rate on Canada. In April, 56% of U.S.-bound Canadian exports were registered under the agreement, up from 50% in the month prior. For context, it's been estimated that between 80-90% of trade can be compliant, as rules of origin allow for 'home-grown' products / industries (i.e., those goods that have content predominantly originating in North America) to be registered under USMCA. Varying degrees of compliance across sectors (Chart 6), economic exposures to U.S. trade, and changes to product-specific tariffs (like steel and aluminum) means that it's an uneven playing field for Canada's provinces – the largest of which (i.e., Ontario) faces the highest effective tariff rate today (Chart 7).

For the **Bank of Canada**, which left policy unchanged yesterday, tariffs are likely to slow growth and continue to damage the labour market, especially in key sectors and provinces with outsized exposure (i.e., Ontario). As retaliation remains relatively muted, and USMCA compliance broadens, it's our view that inflation will remain contained in Canada, giving the Bank the green light to further reduce their target for the overnight rate to 2.00% by year-end. Meantime, the Fed will have a more difficult time contending with tariff-led inflation, which should keep them on the sidelines until Q4, where we see them providing 50bps of rate relief, in-line with the most recent dot-plot.

Chart 1: Tariff revenues are collected at a lag, unlikely to reflect 'peak' levies implied by the U.S. administration

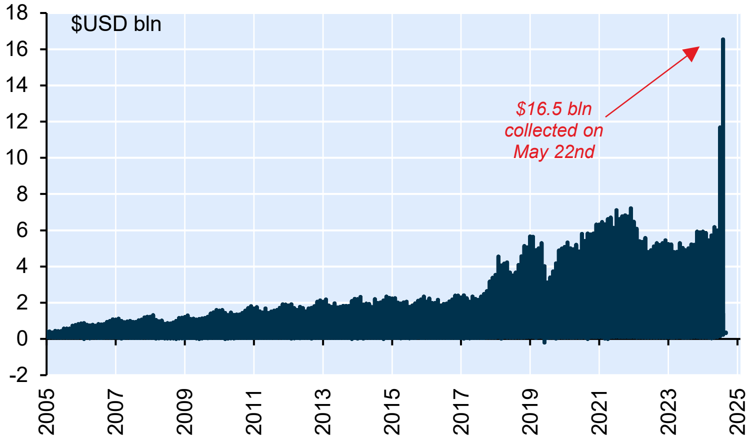
Evolution of the U.S. average effective tariff rate (AETR), 2025 YTD as implied by White House announcements vs as implied by customs revenues



Source: NBC, U.S. Census, Bloomberg | Note: Using 2024 trade weights by country / HS2 code. Customs revenue-implied AETR takes 1M trailing revenue sum and applies this to the monthly import level to arrive at a rate. Where import values are not available, NBC forecast is used. Red data labels denote an escalation in the AETR, while green signals a de-escalation.

Chart 2: Tariff revenues record first post-Liberation spike…

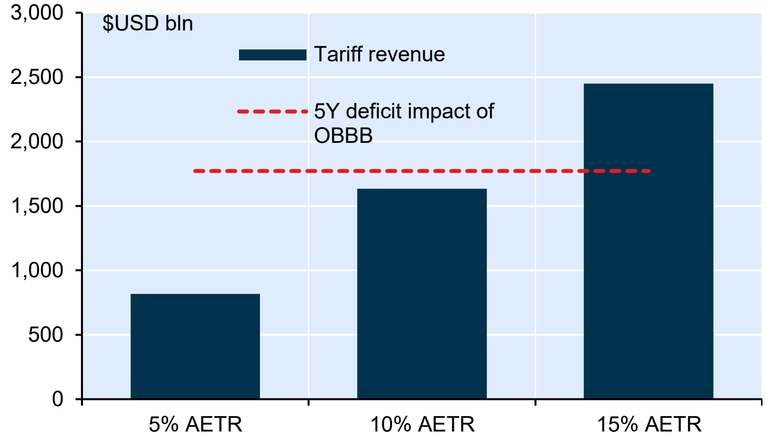
U.S. Treasury deposits – customs & certain excise taxes (daily tariff revenue)



Source: NBC, Bloomberg

Chart 3: … which could help offset new red ink from tax bill

Illustrative tariff revenue and deficit impact of the 'One, Big, Beautiful Bill'

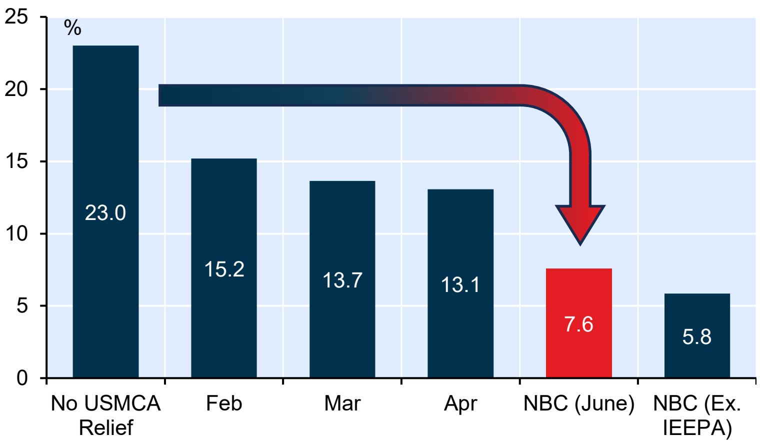


Source: NBC, U.S. Census, CBO

Customs revenues jumped at the end of May, as the April deadline for importer payments was reached. The collections signal a rising AETR, which, if sustained, could help offset impacts from the proposed tax bill. The **CBO** noted that current tariffs could reduce the deficit by $2.8 trillion over the next ten years and forecasted $2.4 trillion in marginal red ink associated with the '**Beautiful Bill**'.

Chart 4: In Canada, USMCA is a key source of tariff relief…

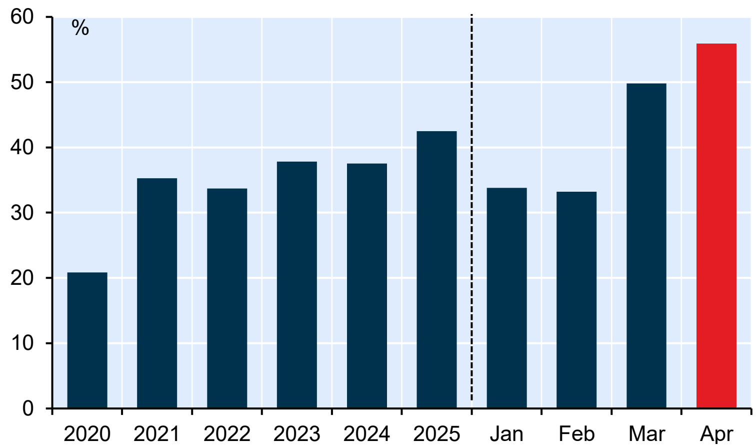
U.S. effective tariff rate on Canadian exports under varying compliance scenarios



Source: NBC, U.S. Census | Note: Using 2024 trade weights with monthly compliance rates

Chart 5: … as compliant trade continues to grow in its share

U.S. imports from Canada under the USMCA / U.S. total imports from Canada

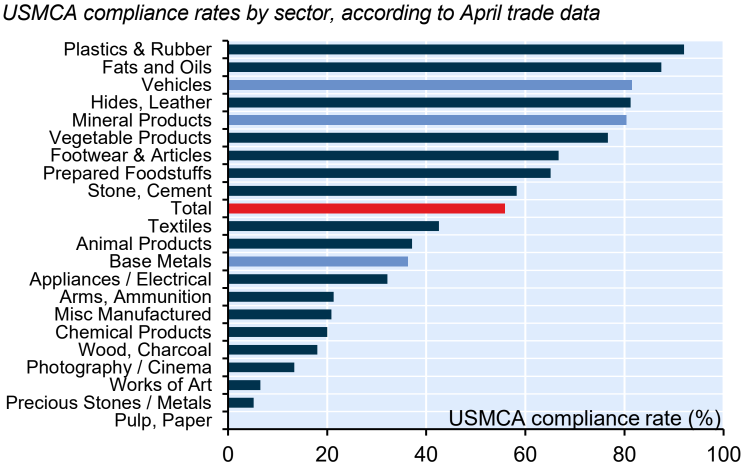


Source: NBC, U.S. Census | Note: 2025 is YTD (Jan-Apr)

While a trade deal between Canada and the U.S. is highly sought / anticipated, the USMCA remains the largest avenue to tariff relief for now. If not for the trade agreement, Canada would be exposed to an effective average tariff of over 20%. As USMCA compliant trade broadens, Canada's exposure should continue to decline – this would be accelerated with the lifting of IEEPA levies.

Chart 6: 'Home-grown' industries are quicker to comply…

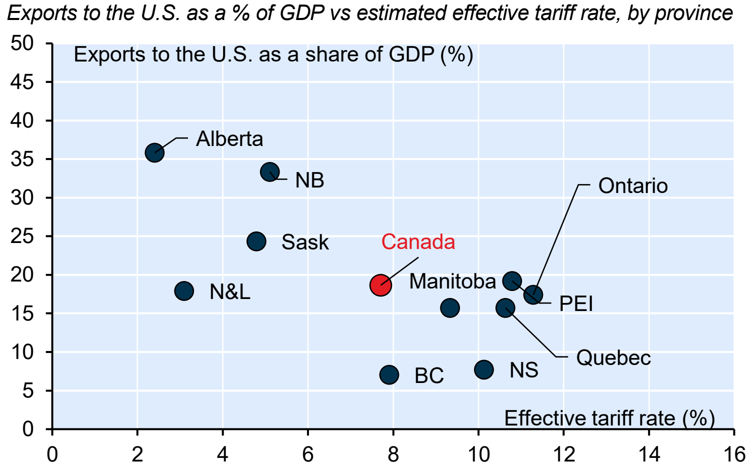
USMCA compliance rates by sector, according to April trade data



Source: NBC, U.S. Census | Note: Aggregates 99 HS2 codes into commonly used 'sections'

Chart 7: … as provincial exposures remain top-of-mind

Exports to the U.S. as a % of GDP vs estimated effective tariff rate, by province



Source: NBC, StatCan | Note: Using 2024 trade weights, StatCan industry data

In April, nearly 60% of U.S. imports from Canada were registered under the USMCA – that's a significant step-up in the past few months, as January's compliance rate was 34%. Some key product groups (highlighted light blue in Chart 6) have rushed to compliance, mineral fuels (i.e., oil) now 80% compliant, relative to under 20% in February. As the trade basket in each province looks different, so too does the relative tariff exposure – this is highlighted in Chart 7, where the effective tariff rate that Ontario faces has climbed due to sector-specific levy increases.

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