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Who's Subsidizing Whom?

Myth and Reality about the Canada-U.S. Trade Balance

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January 2025

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The author acknowledges, without implication, helpful input from Dan Ciuriak, Angelo DiCaro, Stuart Trew, and Erin Weir.

I. Summary and Key Findings

U.S. President-elect Donald Trump has pledged to impose immediate across-the-board 25% tariffs on imports from Canada and Mexico, higher tariffs on imports from China, and universal 10% tariffs on imports from other countries as soon as he is inaugurated later this month. The tariff threat has been widely interpreted as a means of exerting leverage over other countries on a range of trade and non-trade matters (ranging from border issues, to defense spending, to taxes and regulations imposed on U.S.-based tech giants by other countries). Some reports suggest the Trump transition team may soften or narrow its approach before inauguration (Cox, 2025), others suggest he is preparing to implement these threats immediately – even invoking a "national economic emergency" to activate special presidential powers (Lawder and Tanna, 2025). In any case, Trump's actions during his first term in office (from 2016 through 2020), and his generally aggressive and unpredictable approach to governing, mean that Canadians must take his threat very seriously. The impact on Canadian employment, production, and exports from a major across-the-board tariff imposed on our sales to the U.S. (which constitute the large majority of our exports) would be devastating, almost certainly causing a protracted recession.[1] The fact that this threat is being made at a moment of political division and uncertainty in Canada makes it all the more dangerous.

It is important for Canadian trade negotiators, and Canadians more generally, to understand the real economics of the U.S. trade balance, and the full dimensions of the Canada-U.S. economic relationship. In particular, Trump's claim that the U.S. deficit in merchandise trade with Canada amounts to the U.S. "subsidizing" Canada (Crawley, 2024) has no economic merit. It ignores many crucial ways in which the bilateral relationship strongly benefits the U.S., including:

i) Canada is the largest market in the world for U.S. exports, purchasing $440 billion in U.S.-made goods and services in 2023.
ii) The Canada-U.S. trade relationship is among the most balanced of any major U.S. trading partners. The U.S. sells 92 cents of exports to Canada for every dollar it imports from Canada – compared to less than 80 cents in its overall global trade.
iii) The bilateral trade deficit with Canada ranks 10th among U.S. trading partners, accounting for only 5% of the total U.S. trade deficit.
iv) America's bilateral deficit with Canada is much smaller than the $200 billion Trump has claimed. It was $40 billion (U.S.) in 2023 according to U.S. data, 29% less than the 2022 deficit. It fell another 9% during the first 9 months of 2024.
v) The U.S. enjoys a strong surplus in services trade with Canada, which offsets much of the deficit on merchandise trade – and which is only partially reflected in official trade statistics.

[1] Several forecasters have estimated severe consequences from a U.S. tariff; for example, see Canadian Manufacturers and Exporters (2024), and Tapp and Tombe (2024).

vi) The U.S. also enjoys a net surplus on investment income flowing out of Canada ($13 billion Cdn. in 2023), which further offsets the impact of the trade deficit on the overall balance of payments.

vii) Most Canadian exports to the U.S. are inputs used by American businesses in their own production – more so than with other trading partners. Tariffs would thus increase costs for U.S. producers, reducing their competitiveness (including in export markets).

viii) Canadian energy exports (including oil, gas, coal, and electricity) have accounted for 60% of the total bilateral merchandise trade deficit over the last decade, and an even larger share of the total trade deficit (including services). Having access to a secure and lower-cost energy source is a major benefit for U.S. businesses and consumers. And Canada's oil and gas sector, unlike most petroleum exporting countries, is uniquely open to foreign investment. At present U.S. firms own $55 billion in foreign direct investment in Canada's petroleum sector, investments which have been highly profitable.

ix) The bilateral trade deficit with Canada in recent years has been fully offset by Canadian purchases of U.S. bonds and other debt instruments. In effect, Canadian investors are "subsidizing" the U.S. to continue consuming more than it produces. Moreover, low interest rates on that lending mean that the U.S. still enjoys a net surplus on investment income with Canada, despite its net debt to Canada.

Trump's claims that Canada is benefiting unfairly from the bilateral relationship, and is in fact subsidized by the U.S., are false – and Trump's economic team certainly knows it. The U.S. benefits as much from the bilateral relationship as Canada. Indeed, in at least three ways Canada is clearly subsidizing the U.S., through trade arrangements that diverge from normal international trade or business practices, including:

1. Large shipments of secure, lower-cost energy, with unique opportunities for U.S. companies to invest in and profit from those exports.
2. Large Canadian net imports of services from the U.S., many of which (such as digital, streaming, and data services) are weakly regulated, underreported, and largely untaxed (and thus subsidized relative to other businesses).
3. Low-interest loans provided by Canadian investors that have provided the U.S. with purchasing power fully equivalent to the cumulative bilateral trade deficit over the past decade, yet despite which Canada continues to incur a large net deficit in investment income. It's as if a borrower got a large loan from a bank, and then received interest payments *from* the bank (rather than the other way around).

In aggregate, the U.S. would be harmed by disruptions to this bilateral relationship as much as Canada. And while that harm would be dispersed across a much larger economy and population (and hence not be as proportionately disruptive), significant regions and sections of the U.S. economy (including border states, energy-importing regions, and key cross-border industries like automotive manufacturing) would suffer greatly from Trump's proposed actions.

Trump's threats are being used to create leverage in forthcoming trade negotiations, intimidate Canada (and other allies, including Panama and Greenland), and foster an image of aggressive foreign policy for domestic U.S. political consumption. Even more worrisome is increasingly explicit interference by Trump and his advisors in Canadian democracy,[2] exploiting legitimate Canadian concern over the potential impact of U.S. tariffs to effectively promote right-wing politicians here. Trump seemed to claim credit for forcing Prime Minister Trudeau from office with his threat to impose tariffs (Malone, 2025), and then threatened to use "economic force," including his threatened tariffs, to achieve the annexation of Canada (Schmunk, 2025).

Canada has always faced a fundamental challenge in managing affairs with its larger southern neighbour. Today's challenges confirm that neither the 1989 Canada-U.S. Free Trade Agreement, which purported to protect Canada against unilateral U.S. actions (in return for various concessions, including guarantees regarding continental energy supply), nor its successor deals (the NAFTA in 1994, and the CUSMA in 2020) protect us from arbitrary U.S. actions. Trump's threats confirm the incoming U.S. leadership feels no obligation whatsoever to uphold these treaties (which clearly prohibit unilateral actions such as he is proposing).

Acknowledging that the U.S. possesses substantial leverage in coming discussions by virtue of its size, and the fact that disruptions in trade would hurt Canada proportionately more, does not mean accepting Trump's false economic claims. To the contrary, knowing that the U.S. has much at stake in continuing economic cooperation with Canada can empower Canadian negotiators – and the Canadian public – to resist his intimidation. Of course, superior economic logic can't stop a bully from exercising their power. But having accurate knowledge of what's at stake for the U.S. in a trade war helps Canada to construct a more credible deterrence to that bullying.

The rest of this report is organized as follows. The next section provides a brief introduction to the economics of trade balances: how trade surpluses or deficits arise, their consequences, and the costs and benefits of alternative methods of managing them. This makes it clear that the long-standing U.S. trade deficit (which has in fact diminished in recent years relative to U.S. GDP) has little to do with purported structural or competitiveness imbalances (and especially not with Canada). Rather, the U.S. deficit mostly reflects macroeconomic and capital market determinants. The next section then reviews several empirical dimensions of the Canada-U.S. trade balance, including:

i) Canada's importance as the largest U.S. export market, and the relatively balanced nature of Canada-U.S. trade;
ii) The U.S. advantage in services trade (not fully reflected in official trade data);
iii) The composition of Canadian exports to the U.S., and their strategic importance to the competitiveness and success of U.S. businesses;
iv) The unique structural role of Canadian energy exports to the U.S., which account for most of the bilateral imbalance; and

[2] As documented, for example, by Holcroft (2024) and Zakrzewski (2025).

v) The contributions of Canadian investors to the capital flows which have facilitated both strong U.S. purchasing power and the sustainability of the U.S. trade deficit.

The conclusion of the report considers the implications of this data for Canadian trade strategy. Mutual understanding of how a trade war would genuinely hurt both sides is crucial in leveraging the power of deterrence and attaining a more successful, hopefully constructive outcome.

II. How Trade Balances Work

The balance of trade measures the difference between the value of a country's exports, and the value of goods and services it imports from other countries. A trade surplus indicates more exports than imports; a trade deficit represents the opposite. Trade includes both merchandise (tangible products that cross borders) and services (performed by someone for a customer in another country). Some countries (like the U.S.) regularly incur trade deficits; others (like China, South Korea, and Germany) regularly generate trade surpluses. Canada alternates between surpluses and deficits; we experienced a string of surpluses from 1993 through 2008, then 12 consecutive deficits between 2009 and 2020, and have generated small trade surpluses since 2021.

Several factors influence a country's trade balance, including:

- *Competitiveness*: If a country's products are relatively appealing in international markets (because of quality or price factors), it will be able to sell more of them (boosting exports). At the same time, its domestic consumers will be less likely to choose imports. Countries with strong advantages in innovation, technology, productivity, or costs will tend to experience trade surpluses.
- *Exchange Rates*: Fluctuations in exchange rates, which may cause relative prices of exports and imports to diverge from fundamental production costs, may also influence trade balances. A stronger exchange rate makes a country's products more expensive to foreign buyers, and also reduces the relative cost of imports in domestic markets, leading to a larger trade deficit.
- *Trade Policy*: Rules regarding tariffs, quotas, and other regulations affecting trade may affect both the quantity of trade (trade restrictions usually reduce trade in either direction) and its net balance. Most trade agreements endeavour to reduce barriers on both sides of a trading relationship, and hence may have little impact on trade balances; however, unbalanced or unilateral changes in trade rules may have differential effects on trade partners and hence alter trade balances.
- *Macroeconomic Conditions*: A country's purchases of imports will depend on the state of aggregate demand and growth in its own economy: a booming economy will tend to draw in more imports, as both consumers and businesses purchase goods and services from foreign producers. For this reason, a trade deficit can be a sign of strong domestic conditions.
- *Capital Flows*: Trade deficits must be 'paid for': when a country imports more than it exports, it must receive purchasing power from abroad to cover the difference. This can occur in several different ways, and is reflected in changes in the country's international

investment position. By definition, a country's current balance of payments[3] must be fully offset by an opposite balance in international capital flows: a trade deficit must be financed by a net inflow (or surplus) of capital, effectively borrowed from foreign lenders to 'pay for' the net inflow of imports. International capital flows take various forms, including foreign direct investment, equity and bond purchases, and bank borrowing. In general, countries with ongoing trade deficits borrow from the rest of the world and accumulate more international debt; countries with ongoing trade surpluses lend to the rest of the world, and accumulate more net international assets.

These interacting and simultaneous influences make it impossible to definitively explain trade imbalances in any universal way. In some cases, causation runs from trade balances to capital flows: a country with very strong competitiveness will generate trade surpluses, which then become embodied through capital outflows in growing holdings of international assets. In other cases, causation runs from capital flows to trade balances: an autonomous inflow of foreign capital can translate into more domestic demand than would otherwise be justified by domestic production, resulting in a trade deficit.

In many circumstances, a trade deficit is a sign of economic success, not failure. For example, if a major capital inflow consists mostly of new direct investment entering the country (as foreign companies seek to exploit favourable domestic conditions), the resulting trade deficit would correspond to strong economic growth – and, indeed, would be needed to concretely supply the tangible capital goods necessary for those new business investments.[4] Similarly, if a country's domestic economy was growing more vibrantly than its trading partners, it would tend toward deficit in international trade; those deficits, in turn, would help to 'spread' the stimulative impact of that growth to the broader global economy. As noted below, this has been an important factor in recent U.S. trade deficits.

A country with a chronic trade deficit could invoke various policies to reduce its international imbalance. It could adjust trade policy to shift the relative competitiveness of domestic versus foreign products: imposing tariffs, depreciating the domestic currency, or negotiating trade agreements favourable to domestic producers. It could endeavour to improve the underlying competitiveness of domestic production without invoking trade policy levers – through measures to foster innovation or productivity, or (less favourably) by suppressing domestic labour costs or weakening environmental regulations. It could also adjust macroeconomic conditions: reducing domestic spending (to suppress import purchases, perhaps through higher taxes), and increasing national saving (by reducing consumer or government debt). It could also

[3] The overall balance of payments consists primarily of the trade balance, but also includes other flows of current income, including investment income (profits and interest on foreign investments) and transfer payments (such as personal transfers made by migrant workers to family members in other countries).

[4] This was a factor in trade deficits which Canada experienced in the initial postwar decades, as incoming foreign investment fueled rapid economic growth and industrial development.

discourage foreign capital inflows, thus curtailing the means of purchase required to finance trade deficits. All of these policy remedies come with potentially negative side-effects.

Another key factor in understanding bilateral trade imbalances (such as between Canada and the U.S.) is the complexity of trade in a multilateral global trading system. A deficit in trade with one trading partner cannot directly be interpreted as a sign of general trade weakness, depending on how that trade relates to trade flows with other partners. The final impact of a bilateral deficit on a country's overall trade balance depends on the nature and composition of that specific bilateral trade, and its relationship to other trade and investment patterns. For example, a country might import substantial quantities of raw materials or intermediate products (such as energy or manufacturing parts) in order to produce other commodities (such as finished manufactured goods), that in turn are exported to other countries. A country would thus experience a bilateral deficit with one partner (due to unfinished imports), potentially offset by bilateral surpluses with other countries (driven by finished exports). This is highly relevant in the Canada-U.S. case, since most U.S. imports from Canada are not finished products, but rather are inputs used by American businesses in producing other products (some of which are exported, including back to Canada).

These complex and often-contradictory determinants of trade balances are critical to understanding the American trade deficit. The U.S. has incurred a deficit in international trade in goods and services for 49 consecutive years – and it is a foregone conclusion that this streak will reach 50 in 2025. The last time the U.S. generated a trade surplus was 1975. The deficit for 2023 was $945 billion (U.S.).[5] Year-end figures for 2024 (to be published in coming weeks) will likely show it exceeding $1 trillion (U.S.).

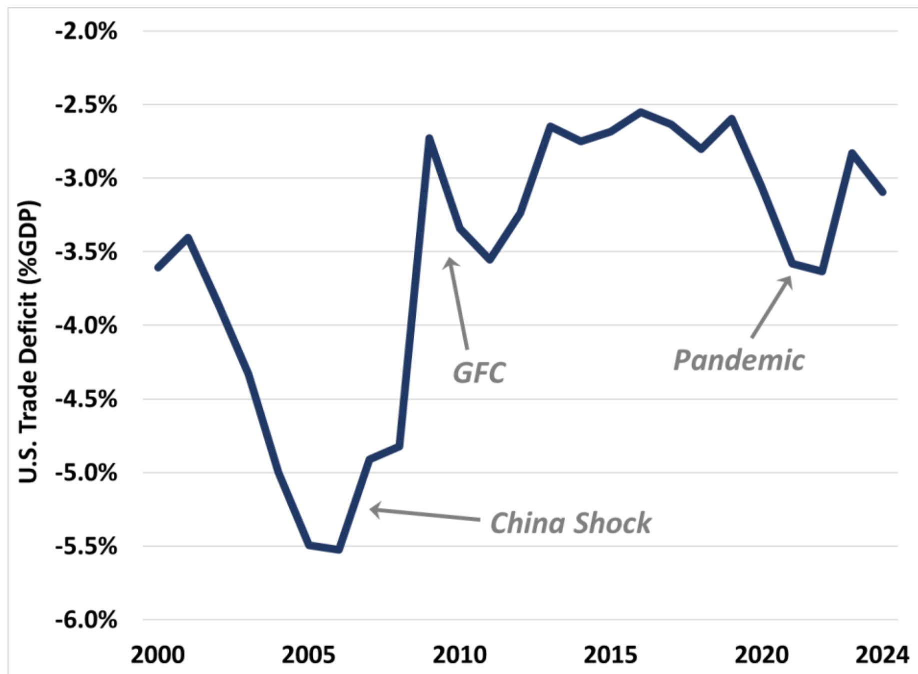
Measured in nominal dollars, the U.S. trade deficit increases almost every year, driven mostly by economic growth, population growth, and inflation. However, relative to the size of the overall U.S. economy, it has fluctuated. Since the turn of the century, the American trade deficit has averaged 3.5% of U.S. GDP. Last year's deficit (just over 3% of GDP) was somewhat smaller than typical of recent history, and barely half the size of record deficits incurred in the mid-2000s (see Figure 1). This long-standing deficit is not new or unexpected, and certainly cannot be described as a "national emergency" as claimed by Trump officials (who are reportedly considering invoking emergency powers to justify unilateral tariffs[6]). According to U.S. trade data,[7] bilateral trade with Canada accounts for just 5% of the overall U.S. deficit.

[5] U.S. BEA NIPA Table 1.1.5.

[6] As reported by Lawder and Tanner, 2025.

[7] Calculations from U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20.

Figure 1. U.S. Trade Deficit, 2000-2024



Source: Calculations from U.S.BEA, National Income and Product Accounts, Table 1.1.5.
2024 data for first 3 quarters.

Recent U.S. trade deficits corresponded with strong economic conditions in the U.S. – much stronger than virtually any of its major trading partners. Economic growth, employment, and real incomes have all grown very strongly in the U.S. since the re-opening of the world economy after the COVID pandemic. Far from causing economic weakness in the U.S., it is clear that the trade deficit is, to a significant degree, a *consequence* of American economic *strength*. With much faster growth in purchasing power, the U.S. expansion was a magnetic draw for imports, whereas sluggish economic growth elsewhere (including in Canada and the E.U.) suppressed growth in U.S. exports.

A major factor in that strong U.S. economic expansion has been a large government budget deficit. The U.S. federal government deficit equaled almost 7% of GDP in the last year[8] – proportionately several times larger than Canada's federal deficit. In addition to stimulating domestic growth and purchasing power, this deficit also corresponded to large capital inflows to the U.S., in the form of foreign purchases of U.S. government bonds. Global financial uncertainty in the wake of the COVID pandemic also reinforced foreign appetite for U.S. bonds, which are considered a secure asset. Therefore, via both macroeconomic channels (the pro-cyclical impact of strong growth on imports) and the capital account (the impact of large capital inflows, which mirror and effectively 'pay for' a current account deficit), recent U.S. trade deficits are a symptom of success, more than a cause of failure.

[8] Calculations from U.S. BEA NIPA Tables 1.1.5 and 3.2.

Economic policies proposed by Trump will have conflicting and contradictory effects on the trade deficit. His spending and tax measures will lead to an increase in the already-large federal budget deficit. This will both strengthen U.S. aggregate demand (drawing in more imports), and require still more foreign borrowing (driving a larger capital inflow, the mirror image of the trade deficit). Most forecasters expect these measures to result in interest rates being kept higher, for longer. With interest rates falling in most other industrial countries (including Canada), this will reinforce financial inflows to the U.S., as investors seek to profit from higher U.S. interest rates. This in turn will lead to a strengthening U.S. dollar (already occurring versus the Canadian dollar and most other currencies), further discouraging U.S. exports and promoting imports. His trade policies (including threatened tariffs) would swim against this tide, trying to shift demand away from imports and toward domestic production (although a stronger U.S. dollar, lifted both by higher interest rates and the tariff itself, would neutralize much of its impact effect). The outlook is complicated further by the unintended consequences of tariffs for U.S. businesses which use imported inputs in their own operations; tariffs could damage the competitiveness of U.S. businesses (including for sales to export markets), not just foreign firms. They will also lead to higher prices in the U.S., hence reinforcing pressure for higher interest rates. Of course, America's trading partners are likely to respond to U.S. tariffs with their own tariffs or countervailing measures, offsetting the impact of the Trump tariffs on U.S. competitiveness.

For all these reasons, it is unlikely that unilateral U.S. tariffs, even if the Trump administration goes ahead with them, would reduce the U.S. trade deficit. In the context of other Trump economic policies, it is more likely the U.S. trade deficit will widen under his policies, not shrink. During Trump's first term in office (2016 to 2020), there was no significant change either direction in the U.S. deficit measured as a share of GDP, despite his "America-first" polices and the (more targeted) tariffs that he implemented.

Trump's focus on tariffs and the trade deficit is clearly motivated more by politics (and perhaps geopolitical designs) than economics. The U.S. trade deficit has decreased, not increased, relative to recent history. Trump's overall economic package (including a larger government deficit and likely higher interest rates) will lead to a larger trade deficit. Canada accounts for a very small share of it. Across-the-board tariffs would have unclear and potentially negative net impacts on U.S. businesses, and the side-effects of those tariffs (including macroeconomic damage to major U.S. trading partners) would be painful for Americans. Knowing this, and showing the U.S. side that we know it, will be important in buttressing Canada's bargaining position in the coming difficult negotiations.

III. The Statistical Reality of Canada-U.S. Trade and Investment

Trump's tariff threat aims to put bargaining pressure on U.S. trading partners regarding other issues (like border, defense, and tax policies). This is reinforced by the political optics of being seen to be 'tough' in dealing with other countries. His recent comments seem to indicate grand imperial designs to literally expand the U.S. In this worrisome context, it is especially important for Canadian negotiators to have a clear and evidence-based understanding of the U.S. trade deficit, its causes and consequences, and the likely impacts of tariffs for the U.S. economy and U.S. businesses.

The size of the U.S. economy, and the disproportionate importance of trade with the U.S. to the economic fortunes of its smaller trading partners, gives the U.S. an inherent power advantage in trade negotiations. But assuming that U.S. negotiators also understand how the U.S. economy works (including the reality of how trade balances are determined),[9] understanding those benefits is important in realistically evaluating whether the U.S. would actually follow through on its threats. And publicly communicating those benefits (including to the Canadian public) is important in strengthening national resolve to confront Trump's tariff threat more confidently and effectively.

To that end, this section considers several underreported dimensions of the Canada-U.S bilateral economic relationship. They place Trump's complaints about America's trade deficit with Canada in perspective. Better understanding of these dimensions – both among Canada's negotiators, and the Canadian public, which has been implicated through both domestic political turmoil and interference from senior Trump officials – is critical for strengthening Canada's bargaining position in the challenging discussions that lie ahead.

America's Trade with Canada is Large and Relatively Balanced

Despite the rapid growth of emerging economies (like China and Mexico), Canada still ranks as the largest U.S. trading partner, with over $900 billion (U.S.) in total two-way trade in 2023.[10] More to the point for upcoming trade negotiations, Canada is by far the largest market for U.S. exports (Figure 2). Canada's purchases of U.S.-made goods and services totaled $441 billion in 2023, according to official U.S. data. That accounted for close to 15% of total U.S. exports that year. U.S. exports to Canada were 20% higher than exports to Mexico, and more than twice as large as U.S. exports to China. Disruptions to U.S. exports to Canada would thus have a major impact on a wide range of U.S. regions and economic sectors.

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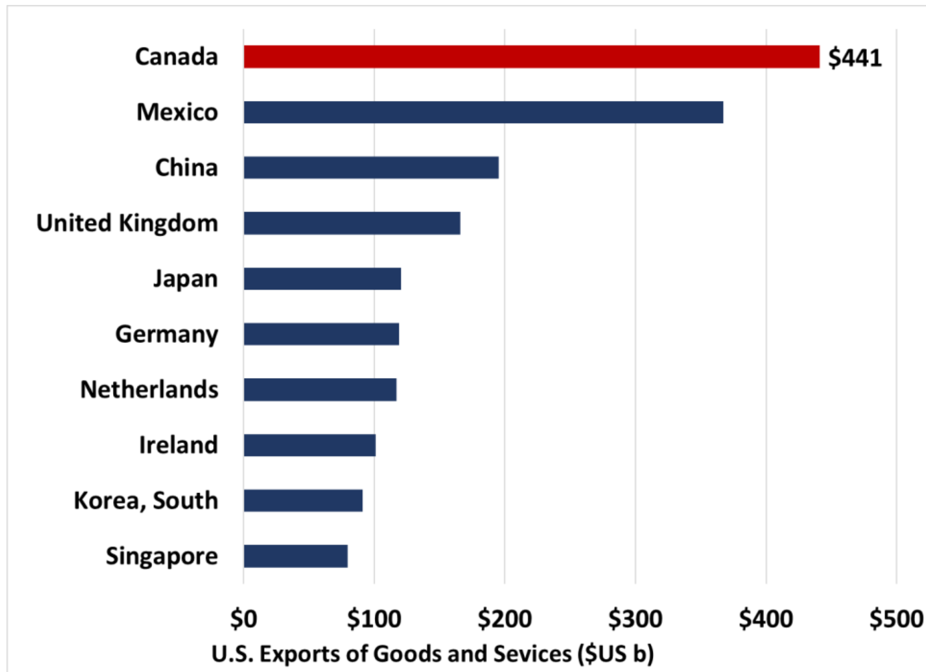
[9] The alternative is to assume that Trump's economic policies are irrational, and that he and his team do not understand what is in the U.S. best interests; while perhaps tempting at times, this hypothesis is far-fetched.

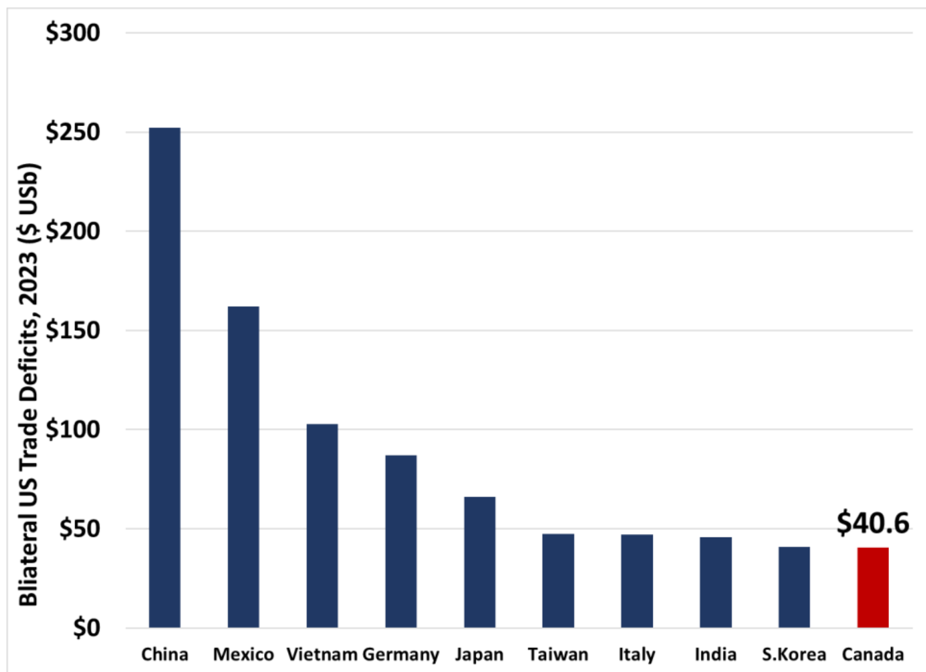
[10] Data in this section from U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20.

Figure 2. Major U.S. Export Markets, 2023



Source: U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20.

Figure 3. U.S. Bilateral Trade Deficits, 2023



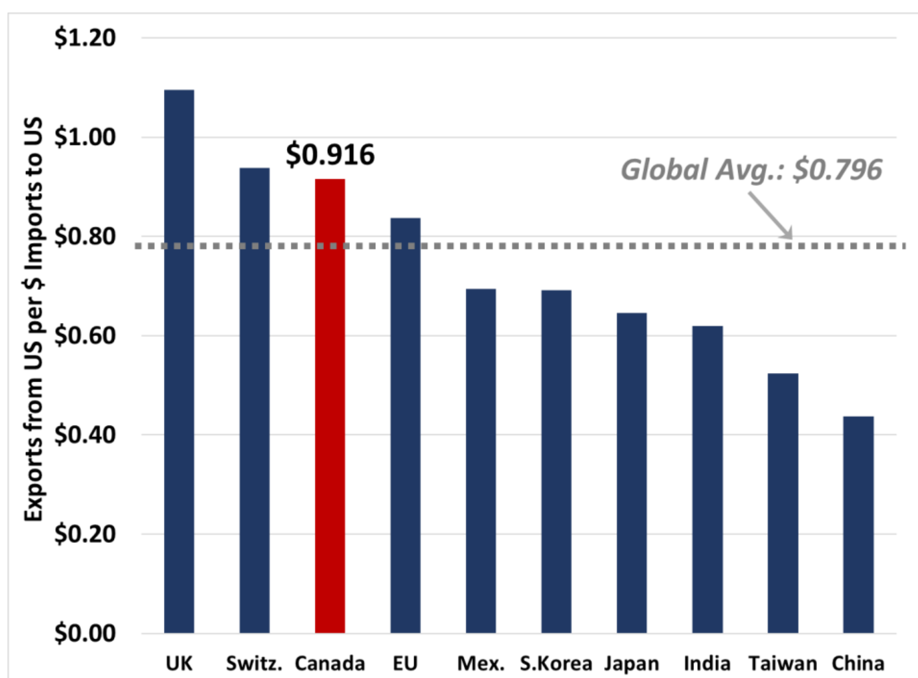
Source: U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20.

While America's exports to Canada are larger than any other country, America's bilateral trade deficit with Canada is relatively small (Figure 3). The deficit equaled $40 billion (U.S.) in 2023, ranking tenth among U.S. trading partners. Recently, the bilateral U.S. trade deficit with Canada

has declined significantly. It shrank 29% in 2023, and over the first three quarters of 2024 (most recent data at time of writing) it declined by another 9% (relative to year-earlier levels). This decline largely reflects the fall in the price of oil from 2022 highs; as discussed further below, energy is the main component in the bilateral Canada-U.S. trade imbalance, so the size of that deficit rises and falls with oil prices. In sum, America's bilateral trade deficit with Canada is small, and shrinking – making it all the more illegitimate for Trump to target Canada with tariff threats (and reinforcing suspicion this threat is being used as leverage on other matters).

Canada imports more U.S.-made goods and services than any other country, but the bilateral trade deficit is much smaller than other major trading partners. This indicates that Canada-U.S. trade is relatively balanced, compared to the overall pattern of U.S. trade. In 2023, the U.S. sold 91.6 cents worth of goods and services in Canada, for every dollar that the U.S. purchased in Canadian exports. This compares favourably to proportionately larger imbalances with other trading partners. Figure 4 illustrates the ratio of U.S. exports to imports in each of its ten largest bilateral relationships (treating the EU as an integrated whole).

Figure 4. Ratio of U.S. Exports to Imports in Bilateral Trade, 2023



Source: U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20.

Canada ranks third-highest in U.S. export reciprocity among the top ten U.S. trading partners. In only one of these countries (the U.K.) does the U.S. export more than it imports (with services accounting for more than half of total bilateral trade with the U.K.). The fact the U.S. incurs deficits with most trading partners is a symptom of its overall tendency to deficit (driven mostly by macroeconomic and capital flow factors). The ratio of U.S. exports to imports is 12 percentage points higher for Canada, compared to its overall global trade. Excluding Canada, that measure of U.S. export reciprocity would fall another two percentage points (to below 78

cents per dollar). Hence, assuming that a disruption in trade with Canada at least partially results in more trade with other countries (through a process of trade diversion, a common side-effect of targeted trade actions), the overall proportional imbalance in American trade would get worse, not better – and its global trade deficit could even increase.

America Enjoys a Large Trade Surplus in Services with Canada

Donald Trump's public statements on trade imbalances almost always focus on merchandise trade, including his (exaggerated) statements about the Canada-U.S. trade balance.[11] But trade in services (including commercial and business services, transportation, tourism, and even international trade in education and health care) is increasingly important in total trade. In services trade, U.S.-based companies enjoy strong advantages in global competition – particularly for dominant U.S. companies in the technology and financial sectors. Globally, the U.S. enjoyed a surplus in services trade of over $275 billion in 2023, that will likely exceed $300 billion for 2024. The success of U.S. trade in services offsets a significant proportion (one-quarter or more, depending on measurement) of its deficit in merchandise. Services trade is an important component of the bilateral Canada-U.S. trading relationship, and must be included in any analysis of net benefits from that trade.

International services trade has been growing rapidly in recent years, for numerous reasons: including the general shift toward services in overall economic activity, technological changes which facilitate cross-border commerce in service industries (from call centres to digital streaming), and trade policies which have reduced former restrictions on international investment and business in services industries. One challenge in understanding the impact of services trade is the incomplete and approximate nature of statistics on services trade (Loranger et al., 2018). It is harder to account for cross-border transaction in services (much of which occurs digitally) than to measure cross-border flows of physical merchandise (which is regulated and logged at border crossings). Another factor is the ambiguity of intra-corporate accounting for transactions between non-arms-length subsidiaries of international corporations; intra-firm accounting for items like administration costs, intellectual property charges, and profits can be easily manipulated, often motivated by efforts to reduce corporate tax liabilities (by artificially shifting bottom-line profits to subsidiaries located in lower-tax jurisdictions).

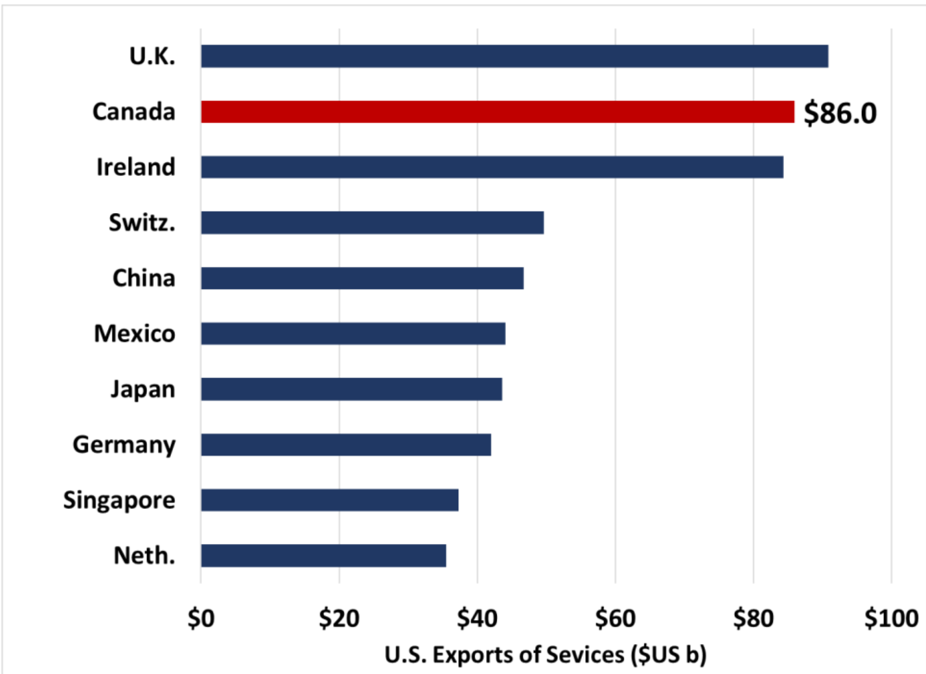
For all these reasons, most economists agree that official data on services trade understates true cross-border transactions by a considerable margin. Cernat (2024) argues that properly measured services trade is now larger than global merchandise trade (in contrast to official statistics, which suggest services account for about one-fifth of global trade). Global Affairs Canada (2022) estimates that services (including services embodied in manufactured exports) accounted for 45% of total Canadian exports in 2017 (whereas conventional data suggests services accounted for just 18% of exports that year). Ciuriak (2023) notes that cross-border flows of data are typically not counted at all, leading to huge undervaluation of services trade

[11] Trump has claimed the bilateral deficit is $200 billion – five times larger than indicated by official U.S. data.

flows. This helps explain the desire of U.S. negotiators to maintain the current unregulated, largely untaxed treatment of global data (much of which is controlled by U.S. tech giants). Wyman et al. (2023) acknowledge that Canada's statistical treatment of cross-border digital services is in its infancy.

Even the official data confirm that services trade is very important in the Canada-U.S. bilateral relationship, and that the U.S. enjoys a significant surplus in that relationship – offsetting much of the U.S. deficit in bilateral merchandise trade. As indicated in Figure 5, Canada is the second-largest export market for U.S. services in the world, behind only the U.K. (with its extensive two-way financial ties to America). U.S. services exports to Canada totaled $86 billion (U.S.) in 2023. They grew 6% year-over-year during the first three quarters of 2024 (most recent data available).

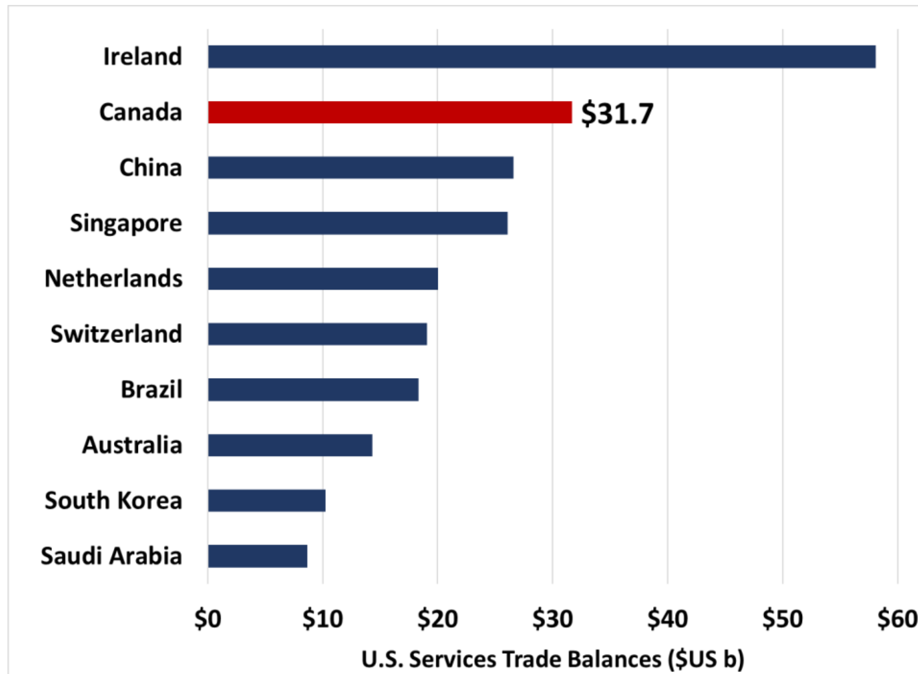
Figure 5. U.S. Services Exports, 2023



U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20b.

Services trade between Canada and the U.S. is not just large, it is also clearly weighted in favour of the U.S. Figure 6 shows that the U.S. services trade surplus with Canada ($32 billion U.S., according to U.S. data) is also the second-largest of any country, behind only Ireland. Keep in mind that services exports to Ireland are artificial, reflecting accounting strategies followed by U.S tech giants (like Microsoft and Apple) to "sell" intellectual property and related services to their own Irish-based subsidiaries (Boller et al., 2024). That allows those firms to take advantage of Ireland's status as a low-corporate-tax jurisdiction within the broader European Union. In contrast, U.S. services exports to Canada more genuinely reflect value-added production, with consequent benefits for jobs and incomes in the U.S. Excluding the tax-avoiding case of Ireland, therefore, Canada is the most important market for net exports of U.S. services.

Figure 6. U.S. Services Trade Balances, 2023



U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 20b.

Table 1 Canada-US Trade in Services, 2023				
	Canada Service Exports to U.S.	**Canada Service Imports from U.S.**	**Balance**	**As % Canada-U.S. Bilateral Merchandise Trade Deficit**
Statistics Canada, Table 36-10-0016-01				
$C billion	$107.2	$121.0	-$13.8	12.8%
$US billion[1]	$79.4	$89.6	-$10.3	
US Census Bureau / BEA, Exhibits 20, 20a, 20b				
$US billion	$54.3	$86.0	-$31.7	43.8%
Source: Calculations from Statistics Canada Table 36-10-0016=01, U.S. Censure Bureau, U.S. International Trade in Goods and Services, Exhibit 20b. 1. Converted at 2023 annual average exchange rate (74.1¢).				

According to U.S. trade data, America's bilateral surplus in services trade with the U.S. offsets 44% of its bilateral deficit in merchandise trade with Canada. Keep in mind that the intangible nature of much services trade, and lack of reliable data, means that services trade statistics do

not fully capture the size and balance of services trade. In contrast, Canadian trade data indicates Canada-U.S. services trade is not as unbalanced as the U.S. data suggests. As shown in Table 1, Statistics Canada data reports Canada's services exports to the U.S. are larger than accounted for in the U.S. data, and as a result the imbalance is smaller: about $14 billion (Cdn.) in 2023. However, it is likely that both sources of data underestimate both the scale of bilateral services trade (for reasons explained above), and the size of the U.S. surplus (especially given U.S. dominance in new, hard-to-measure activities such as data, streaming, e-commerce, digital platforms, and other activities dominated by major U.S. players). Those activities are largely uncounted, mostly untaxed, and poorly regulated.

The incoming Trump administration has pledged to aggressively defend these loopholes: for example, vociferously opposing Canada's new Digital Services Tax. The poor regulation and taxation of these U.S.-produced services (compared to other, more traditional forms of services production) constitutes an effective subsidy by Canadians to hugely profitable U.S. firms. By any measure, the U.S. benefits substantially from its large services trade with Canada, and it is unreasonable to limit trade debates to merchandise alone (as Trump officials tend to do). Indeed, according to U.S. data (which reports smaller services imports from Canada than Statistics Canada), the U.S. bilateral services surplus with Canada was large enough in some years (as recently as 2018) to more than fully offset the bilateral deficit on merchandise trade – producing an overall bilateral trade surplus in America's favour.

While it is not included in the trade balance, another feature of the Canada-U.S. relationship that works in America's favour is the flow of income on capital investments. Cross-border payments of profits, dividends and interest are not counted in the trade balance, but they do constitute an important element of the broader current account balance (along with transfer payments by individuals and governments). Investment income paid from Canada to U.S. investors exceeds investment income repatriated from the U.S. by Canadian owners, with the result that there is a large net outflow of investment income from Canada to the U.S. In 2023, this translated into a net surplus for the U.S. on investment income worth (according to Statistics Canada data) some $13.3 billion.[12] This does not include profits retained by U.S. subsidiaries in Canada (which can use those earnings to expand their equity in their Canadian operations). This net outflow of investment income to the U.S. further offsets (along with the U.S. bilateral services trade surplus) the U.S. bilateral merchandise trade deficit.

The outflow of investment income from Canada is ironic, since for several years (since end-2016) Canada has had a positive net international investment position with the U.S. In other words, Canadians now own more assets in the U.S., than Americans own in Canada. Despite this, Canada still experiences a net outflow of investment income to the U.S. (for reasons discussed further below).

[12] Statistics Canada Catalogue 36-10-0014-01.

Most U.S. Imports from Canada are Inputs to Production by U.S. Businesses

After 35 years of continental free trade, the Canadian, U.S., and Mexican economies are highly integrated. Two-way flows of products and services are a core structural feature of most industries. Supply chains which service businesses in any sector are complex and overlapping. An extreme example is the automotive manufacturing sector: components of an automobile typically cross North American borders several times before being finally installed in a finished vehicle.[13] In this context, it is difficult to define whether a product is truly 'made' in any one of these three countries: all products now embody extensive inputs produced across North America.

Because of this supply chain integration, the large majority of Canadian exports to the U.S. do not constitute finished products. Instead, most Canadian exports flowing south are in turn used as inputs by U.S. firms in their own production of goods and services. By penalizing the inflow of intermediate products essential to U.S. production, it is not at all clear that a unilateral tariff on Canadian products helps U.S. firms. Even more confusing, some of the output of U.S. firms produced with the help of Canadian inputs, is in turn exported to foreign markets (including back to Canada!). By making U.S. production more expensive (due to more expensive imported inputs), a tariff would undermine these U.S. exports and thus worsen the trade deficit that is the (purported) motivation for the tariff. Evidence is clear that these two-ways flows of intermediate products dominate the Canada-U.S. trade relationship.

Table 2
Composition of U.S. Imports, 2023

Category	All U.S. Imports	Imports from Canada
Energy	8.3%	29.1%
Other Industrial Inputs	17.8%	23.5%
Capital Equipment	36.2%	23.4%
Passenger Cars	6.6%	8.1%
Other Consumer Goods and Food	31.1%	15.9%
Total	100%	100%

Source: Calculations from U.S. Census Bureau, U.S. International Trade in Goods and Services, Exhibit 7 (for U.S. total), and ISED, Trade Data Online (for Canada).
Automotive products other than passenger cars are included in capital equipment.

[13] See Klier and Rubenstein, 2008, Ch. 6, for a full discussion.

Table 2 summarizes the composition of U.S. merchandise imports, across several major product categories.[14] It also shows the corresponding composition of U.S. merchandise imports from Canada.[15] It is striking that only a minority of total U.S. merchandise imports (less than 40%, including passenger cars) consist of final consumer products. This reveals that the phenomenon of overlapping international supply chains also applies more broadly to U.S. trade relationships, not just those in North America. But the importance of this trade in unfinished and intermediate products is especially dominant in Canada-U.S. trade.

Energy products (including oil, gas, coal, and electricity) account for almost one-third of Canadian exports to the U.S., compared to just 8% of all U.S. imports. Energy is an input to other activities. There is little rationale for the U.S. to make energy more expensive for its own businesses or consumers. Other industrial materials (including other minerals, basic metals, raw materials, and semi-processed goods) account for another quarter of U.S. imports from Canada – again, significantly more than for overall U.S. imports. Finished products, however, account for a smaller proportion of U.S. imports from Canada, than from the rest of the world. Finished capital goods (such as machinery and equipment) make up less than one-quarter of U.S. imports from Canada, compared to 36% of overall U.S. imports. Those capital goods are also used as inputs in subsequent productive activities. Automotive products are the only finished commodity grouping in which Canada is overrepresented in the profile of U.S. imports: making up 8.1% of imports from Canada, versus 6.6% from the world as a whole. Finished consumer goods (other than passenger cars) make up a small share of Canadian exports to the U.S.: just 15%, half the share for the whole world.

The fact that Canadian and American supply chains are so intertwined creates numerous unexpected and counterintuitive outcomes in cross-border trade. One of them is that Canadian products sold to the U.S. themselves embody significant amounts of U.S.-made content, via imports from the U.S. of intermediate products used in their production. Indeed, about 17% of the value of all Canadian-made merchandise exported to the U.S. was produced in the U.S. – and then imported to Canada, incorporated into a final product, and then sold back to the U.S. (Figure 7). In the manufacturing sector, U.S.-made content accounts for 27% of the value of Canadian exports. By curtailing imports from Canada, a U.S. tariff would directly undermine demand for these U.S.-made inputs, thus offsetting a significant share of the purported benefit for U.S. producers of the tariff. This is another reason why the effects of tariffs on Canada-U.S. trade flow (dominated by intermediate goods) would be very different from tariffs imposed on finished products imported from countries with more independent supply chains.

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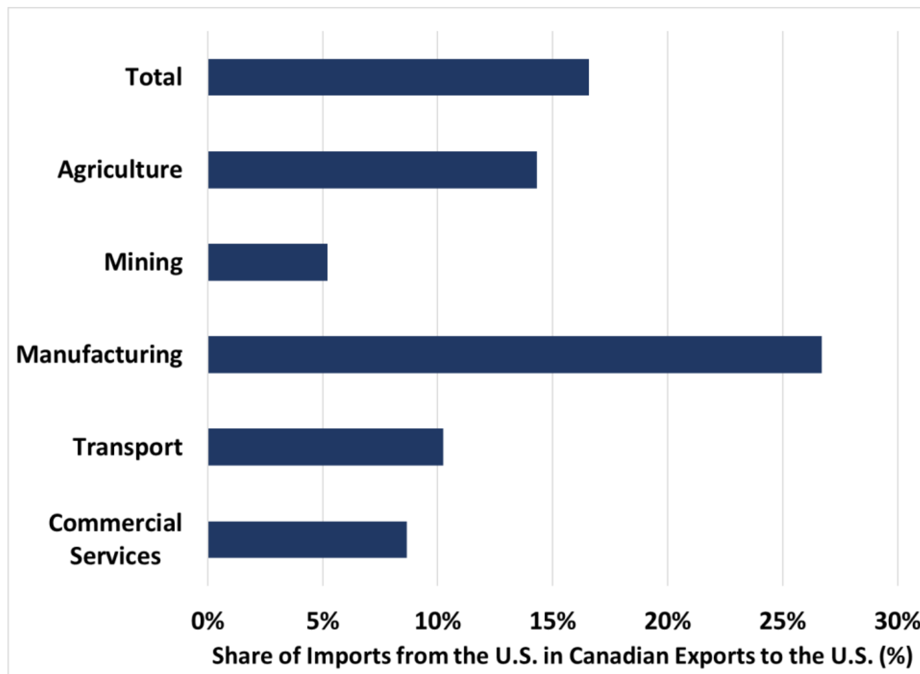
[14] No similar decomposition is possible for services imports, due to incomplete and unreliable data on the scale, nature, and direction of cross-border services transactions. Nevertheless, it is safe to assume that a majority of traded services (especially in rapidly-growing commercial and business services) also constitute intermediate inputs to subsequent (downstream) production, rather than being intended for final consumption.

[15] The Canadian data has been mapped onto the same categories used in the U.S. data for comparison purposes; some of that mapping is approximate.

Figure 7. U.S.-Produced Content in Canadian Exports to the U.S., 2022



Source: Calculations from Statistics Canada Table 12-10-0100-01.

The fact that Canadian exports to the U.S. are so concentrated in intermediate inputs, rather than finished goods, changes the calculus for the U.S. regarding the effects of a tariff. It makes it less likely that a tariff will stimulate domestic U.S. production, and more likely that it will increase U.S. production costs and potentially damage the competitiveness of U.S.-made products (including products intended for export[16]).

Canadian Energy Exports Constitute Most of the Bilateral Deficit

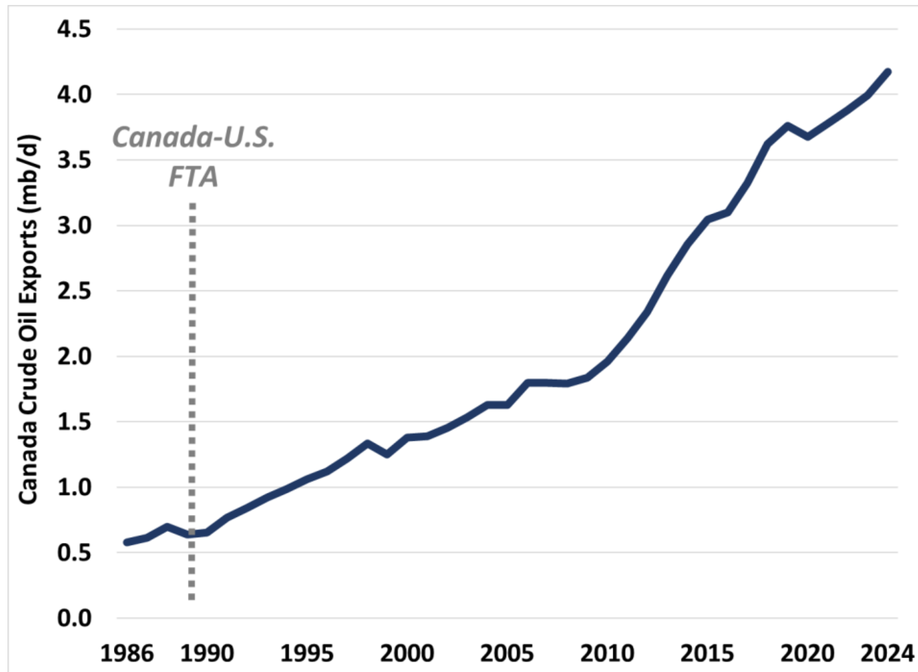
Among all these intermediate imports from Canada, energy plays a particularly important role in the U.S. economy. The largest single export from Canada to the U.S. is energy: over $170 billion worth in 2023, including crude oil, petroleum products, natural gas, coal, and electricity. Crude oil is the largest component of this energy flow, accounting for $130 billion (or three-quarters) of that total in 2023.

Over the last generation, oil exports to the U.S. have increased steadily and dramatically. This surge began in earnest after the implementation of the Canada-U.S. Free Trade Agreement in 1989. That agreement included an unprecedented "proportionality clause", by which Canada committed to continuing to supply energy to the U.S. (in line with historic proportions) even in the event of supply disruption or other emergency. This provision effectively guaranteed the security of Canadian energy for U.S. purchasers (greatly appreciated by Americans after the energy supply shocks of the 1970s). It paved the way for enormous increases in Canadian oil

[16] The flow-through impact of a tariff on U.S. exports could be offset by duty drawback provisions, if they were permitted under whatever unilateral tariffs the U.S. eventually imposed.

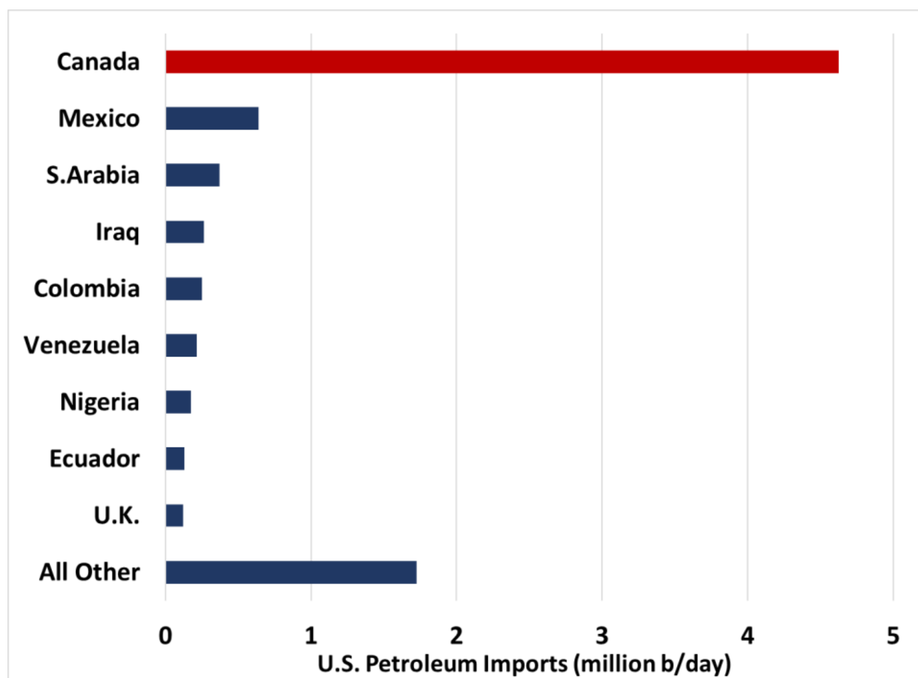
production and export. Over the next 35 years, Canadian oil exports to the U.S. grew eight-fold, reaching 4.2 million barrels per day (almost all to the U.S.) by the first half of 2024 (Figure 8).

Figure 8. Canadian Crude Oil Exports, 1986-2024



Source: Canadian Energy Regulator, Crude Oil Export Summary, Crude Oil Exports by Destination. 2024 data first 6 months.

Figure 9. U.S. Oil Imports by Source, 2024



Source: U.S. Energy Information Administration, Monthly Energy Review. Average for first 9 mos.

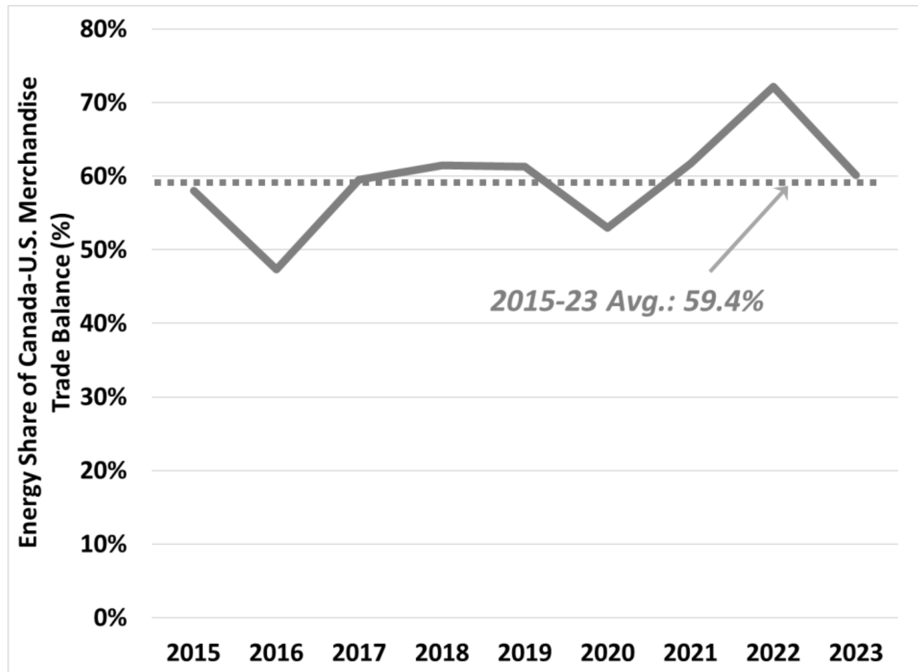
The proportional energy sharing provision was abandoned in the renegotiated Canada-U.S.-Mexico free trade agreement implemented in 2020, but by then the integration of Canadian petroleum into the U.S. energy system (reinforced by extensive investments in north-south transportation infrastructure) was cemented. Canada is now the dominant source of imported oil to the U.S., accounting for 54% of total U.S. oil imports over the first three quarters of 2024 (Figure 9). The risk that energy supplies in the U.S. would be disrupted by conflicts in far-off regions (such as the Persian Gulf) has been largely dissipated by this increasing U.S. reliance on Canadian supplies. Canadian energy is both secure and relatively inexpensive: cheaper thanks to lower transportation costs of shipping from Canada to the U.S., and also the lower quality of Canadian crude supplies (now mostly heavy synthetic crude produced from bitumen). Trump recently claimed the U.S. doesn't need anything from Canada, even oil (Platt, 2025); clearly, that boast is false. A shut-off of Canadian oil exports to the U.S. would spark an energy crisis in the U.S. far worse than any of the supply shocks of the 1970s.

By supplying the U.S. with less expensive and secure supplies of petroleum, that now constitute the majority of U.S. energy imports, Canada is underwriting energy security for the entire U.S. economy. Moreover, Canada offers a rare opportunity for U.S. companies to participate in producing, selling, and profiting from the production and export of another country's petroleum. Canada is one of the only oil-exporting countries in the world which does not have a major state-owned producer; its petroleum sector (following the privatization and deregulation that occurred in the late 1980s and early 1990s, alongside the Canada-U.S. Free Trade Agreement) is uniquely open to private and foreign investment. U.S. firms accounted for $55 billion worth of foreign direct investment in Canadian oil and gas firms in 2023 (over half of all foreign investment in that sector), and those investments have been lucratively profitable in recent years. This combination of secure supply, lower costs, and investment opportunities constitute a major advantage for the U.S. – refuting the claim that the U.S. is subsidizing Canada. To the contrary, America's opportunity to secure a foreign source of non-renewable energy, at favourable prices, and partly owned by U.S. investors, is a stark divergence from normal international patterns of petroleum trade. This more realistically can be considered a "subsidy", compared to the terms of America's other energy supply options.

Because of the importance of energy (especially petroleum) in Canada's exports to the U.S., and the value for the U.S. of Canada's convenient and secure energy supplies, its purchases of energy certainly cannot be interpreted as a favour or "subsidy." Energy accounts for about 60% of America's total bilateral merchandise trade deficit with Canada (Figure 10). It accounts for an even larger share of the total bilateral trade deficit, including services. The importance of energy in the bilateral deficit rises or falls with fluctuations in the price of oil. It made up 72% of the bilateral deficit in 2022 when global oil prices spiked after the invasion of Ukraine, but has fallen back to a traditional share more recently as oil prices moderated.[17]

[17] Weir (2007) shows that the importance of energy in the bilateral trade deficit has been a longstanding phenomenon since the Canada-U.S. FTA.

Figure 10. Canada-U.S. Bilateral Energy Trade Balance, 2015-2023



Source: Calculations from ISED Canada, Trade Data Online. Covers product code HS27.

Canada is supplying a resource that the U.S. presently needs for almost all economic activity, but cannot produce domestically in sufficient quantities. The risks and unintended consequences for Canada of basing its exports so heavily on non-renewable minerals, whose future value will decline as the world moves to renewable energy, have been debated within Canada (including the potentially negative side-effects of petroleum exports for other export industries). But regardless of whether this situation is positive or negative for Canada, there is no doubt that America's vast purchases of this energy are motivated by self-interest, not charity. And the resulting bilateral merchandise trade deficit is an arithmetically inevitable consequence of America's favoured access to Canadian energy. If America couldn't access this petroleum from Canada, it would have to purchase it from Saudi Arabia or other more expensive and less secure producers, resulting in an even larger U.S. trade deficit.

Canadian Investors Help Americans Pay For Imports from Canada

As explained in the first major section of this report, there is a mirror-image relationship between a country's trade balance[18] and net international flows of capital. By definition, a country's aggregate current account and capital account must perfectly offset each other. A current account deficit (typically due primarily to a trade deficit) must be offset by a net inflow of finance from other countries which, in effect, allows the country to 'pay' for the trade deficit. Countries which experience chronic trade deficits (as the U.S. has for the last 49 years) must

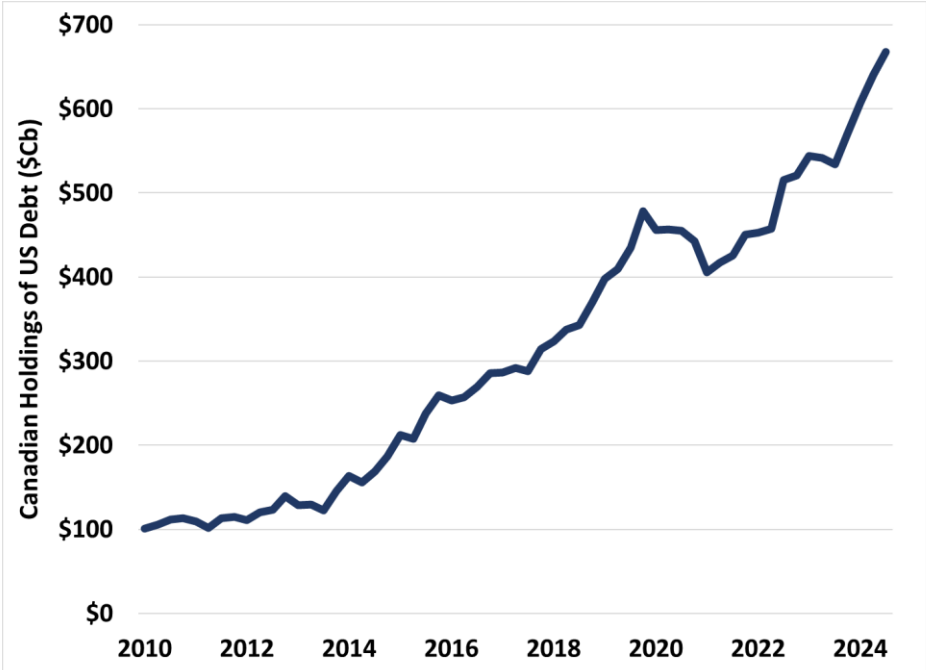
[18] Or, more precisely, its current account balance, including non-trade current flows such as investment income and transfer payments.

mobilize funds from other countries, resulting in accumulating foreign debt. Those capital flows take various forms, including incoming foreign direct investment, incoming portfolio investments, foreign purchases of domestic bonds, or loans from foreign banks.

There is debate among economists about which side of this accounting identity causes which. Some argue that autonomous shifts in capital flows (such as decisions by a country to borrow heavily, or inflows of direct investment by multinational corporations) cause resulting changes in trade balances. Others argue that autonomous changes in trade competitiveness can cause changes in trade balances (positive or negative) which are then reflected in offsetting accumulations or decumulations of international financial assets. The reality is that causation can flow in either direction, depending on the broader economic context.

In any event, the link between trade deficits and international debt is clear in the U.S. case. The persistence of trade deficits over recent decades has been reflected in the growth of America's net foreign debt. By the end of the third quarter of 2024, the net U.S. international investment position reached negative $23.6 trillion (U.S),[19] making America far and away the largest debtor nation in the world. Some economists worry about potential future instability resulting from this foreign debt; others interpret it as a sign of U.S. dominance over the international financial system, and the desire of foreign investors to continue investing in U.S. assets. As usual in economic debates, there is some truth in both these perspectives.

Figure 11. Canadian Holdings of U.S. Debt, 2010-2024



Source: Statistics Canada Table 36-10-0485-01.

[19] U.S. Bureau of Economic Analysis, International Investment Position.

Canadians have certainly done their part to facilitate the financial inflows that allow the U.S. to continue incurring annual trade deficits. As illustrated in Figure 11, Canadian holdings of U.S. debt instruments have more than quintupled since late 2013, reaching almost $700 billion ($Cdn.) by the third quarter of 2024. It is interesting to note that over this 11-year period, new Canadian purchases of U.S. debt instruments (including bonds and Treasury bills) almost perfectly matched the cumulative total of bilateral Canada-U.S. trade imbalances. This is largely a coincidence: there is no reason why a country must seek financial inflows from the same country with which it experiences a trade deficit. Rather, it only needs to mobilize financial inflows from the rest of the world sufficient to offset its global current account deficit. Nevertheless, the fact that Canadian holdings of U.S. debt have increased in tandem with the ongoing U.S. bilateral trade deficit with Canada, puts another perspective on this imbalance. If the U.S. were not accumulating international debt at such a rapid pace (including from Canada), it could not be experiencing corresponding trade deficits (again, including with Canada).

Table 3
Canada-U.S. Bilateral Investment Posititon, 2023

Stocks of Investment (4Q)		
Canadian Investment in U.S. ($t)	U.S. Investment in Canada ($t)	Net Canada Position ($t)
$5.11	$3.96	$1.15
Flows of Investment Income		
From U.S. to Canada ($b)	From Canada to U.S. ($b)	Net Canada Balance ($b)
$112.9	$126.2	-$13.3

Source: Calculations from Statistics Canada Tables 36-10-0485-01 and 36-10-0014-01. Investments measured at market value.

Curiously, despite this large outflow of finance from Canada to the U.S., Canada still experiences a chronic and significant deficit on cross-border flows of investment income (consisting of profits, dividends, and interest payments). This occurs despite Canada now holding a large surplus in its bilateral international investment position with the U.S. (reversing the Canada's historical status as a net debtor to the U.S.). Since 2016, Canadian investors have owned more assets in the U.S., than U.S. investors have owned in Canada.[20] In addition to the large Canadian purchases of U.S. bonds noted above, this shift also reflects years of major Canadian purchases of other U.S. assets – including portfolio investments and direct business and property assets. U.S. investments by Canadian pension funds and other institutional investors have been a major

[20] In the narrower category of foreign direct investment, the switch occurred a year earlier: by 2015, Canadian businesses had more FDI in the U.S. than U.S. businesses had in Canada.

driver of this historic change. As shown in Table 3, by end-2023, total Canadian investments in the U.S. exceeded $5 trillion – $1.15 trillion more than the value of U.S. investments in Canada.

Normally, a net investment surplus should translate into a positive net flow of investment income back to the home country. This was certainly the case for most of Canada's postwar history: over that time, a large U.S. surplus of net investment was accompanied by a large annual net outflow of investment income back to the U.S. (consequently weakening Canada's current account balance). This is not the case, however, in the current bilateral investment relationship: the net flow of investment income still favours the U.S. by a considerable margin ($13 billion Cdn. in 2023, as noted above). This partly reflects relatively low rates of return paid on U.S. government bonds which constitute a large share of Canadian-owned U.S. assets. Because of its status as issuer of the global reserve currency, the U.S. government can issue U.S.-dollar-denominated debt at lower interest rates than other countries; investors purchase those bonds despite low interest rates as a hedge against currency fluctuations and other financial risks.

The end result is that Canadian investors have literally lent Americans all the funds required to pay for their cumulative bilateral trade deficits with Canada since end-2013, yet American investors in aggregate still receive net investment profits from cross-border investment flows. In aggregate, Canadians have lent Americans money to, among other purposes, sustain its chronic trade deficits – but on a net basis, Canadians are paying for the privilege of doing so. It is akin to a bank lending money to a borrower, and then paying that borrower interest (instead of the other way around). This is another surprising feature of the bilateral relationship that should lead observers to ask: Who is subsidizing whom?

IV. Implications for Canadian Trade Strategy

Donald Trump's threats to impose across-the-board 25% tariffs on imports from Canada, in blatant violation of long-standing bilateral and multilateral trade treaties, poses an existential threat to the Canadian economy. Because of the importance of Canadian exports to the U.S., intensified after 35 years of continental free trade (under the same agreements which Trump now ignores), Trump's actions, if implemented, would cause widespread economic dislocation, unemployment, and uncertainty. Even more ominously, his stated intent to use these tariffs as an instrument of "economic force" to achieve annexation of Canada into the U.S. constitutes a clear and dangerous threat to the sovereignty and viability of our country.

There is no easy solution to this problem. The U.S. possesses much greater economic and military power than Canada. While the aggregate costs to the U.S. of a breakdown in Canada-U.S. trade and investment would be as great, or greater, than the aggregate costs to Canada, they would constitute a much smaller proportion of total U.S. economic activity, and hence would not cause the same nation-wide harm. However, in certain regions (such as border states) and industries (such as automotive manufacturing) the pain on the U.S. side would be intense and concentrated. And since the U.S. now relies on Canada for most of its oil imports, a disruption in that flow would have severe national ramifications for Americans.

Obviously, the best solution is a successful negotiation with the U.S. to avoid tariffs, presumably in return for changes in other aspects of Canada-U.S. relations. Those who theorize that Trump's threats are all about creating "leverage" see opportunity in this direction – although even then, the consequences for Canadian sovereignty are worrisome. Once a precedent is set that by threatening economic dislocation, the U.S. can leverage policy actions by Canada in any number of unrelated areas, the whole drama is likely to repeated. Less optimistically, if the Trump administration is indeed pursuing expansionary ambitions, and/or is motivated more by domestic and global power politics than concrete economic self-interest, then the course of the future relationship will be fraught, unknowable, and frightening.

In either case, the evidence provided in this report is important for Canadian negotiators and policy-makers, and for the Canadian public. We can confidently reject claims that the bilateral Canada-U.S. trade deficit is a problem for the U.S. (and it is certainly not an "emergency"). The bilateral deficit is small and shrinking, bilateral trade is far more balanced with Canada than with other U.S. trading partners, and the overall U.S. deficit is driven mostly by macroeconomic and financial factors, not structural problems in U.S. competitiveness. In no way does the U.S. subsidize Canada through this deficit. To the contrary, there are unusual features of the Canada-U.S. relationship that benefit the U.S. in ways that diverge from normal international trade patterns, including:

- Preferential secure access to lower-cost petroleum supplies, with unique access for U.S. investors to profit from its production and export.
- Large inflows of U.S. services to Canada, many of which (especially data, streaming, and platform services) are underreported, weakly regulated, and largely untaxed, shifting a fiscal burden to Canadians.
- Continued flows of low-cost debt finance from Canada to the U.S. (sufficient to offset the cumulative bilateral trade deficit), which coexist incongruently with a net outflow of investment income from Canada to the U.S.; in aggregate, Canadian investors are 'paying' to lend money to Americans so they can continue purchasing more than they produce.

These diversions from normal practice can more reasonably be considered "subsidies." In other words, there is a much stronger case that Canada is subsidizing the U.S. through the bilateral relationship, not the other way around.

Showing that the U.S. benefits from the existing bilateral relationship as much as Canada does, may not convince a bully to stand down. But showing the other side that we are aware of those benefits, and the costs to the U.S. of a potential breakdown in trade, can temper their aggression, and reinforce Canada's bargaining position. Meanwhile, showing Canadians that Trump's claims of "subsidization" are false, and that the bilateral relationship is mutually beneficial, can solidify Canadian support for a fair resolution – vitally important given narrow sectoral or regional vested interests within Canada, and political turmoil at the federal level.

In a worst-case scenario, if Trump's tariffs are imposed (let alone if he mobilizes other weapons of "economic force" against us), then Canada will confront a national emergency. All stakeholders (including governments at all levels and of all political persuasions) will need to respond accordingly with a courageous defense plan. That would need to include aggressive efforts to expand trade links with other countries; equally aggressive efforts to reorient Canadian production around domestic (rather than export) markets; emergency fiscal measures to support domestic spending power and household financial stability in the wake of industrial disruption and unemployment (potentially funded in part with revenues from export taxes and/or tariffs imposed by Canada in the event of a trade war); and a national strategy to build alternative domestically-focused industries (including affordable housing, sustainable energy, and human and caring services) to fill the void left by a downturn in export industries.[21] This is a daunting scenario, but not impossible.

While preparing for the worst, Canadian trade strategists can fight hard for a better outcome. Knowing the truth about the Canada-U.S relationship, and being prepared to speak that truth – both to Trump officials, and to Canadians – can help in that effort.

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[21] Such a plan could be akin to ambitious efforts to rebuild Western economies after World War II; see Stanford (2020) for the continued relevance of that history for recent events.

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