

Canada's economic outlook and global trade: A conversation with Governor Tiff Macklem

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[00:05:16.34] - Adam S. Posen

Hello everyone and welcome back to the Peterson Institute for International Economics. I'm Adam Posen, the Institute's president, and as part of our events with a macro focus around the annual meetings of the Fund and the Bank, I am delighted to welcome to the Institute Tiff Macklem, the Governor of the Bank of Canada. I've known— I've been fortunate to know Tiff for almost 30 years now. I met him when we were doing a study of the inflation targeting regime at the Bank of Canada, but he is well known in central banking and finance circles for quite some time as a leading civil servant internationally, as well as someone who has represented Canada with deep roots in Canada for many years. He first joined the Bank in 1984 and came back in 1989 and occasionally would go off again, including to become Associate Deputy Minister at the Department of Finance. During the global financial crisis in 2008-2009. He returned to the Bank in July 2010 when he was appointed Senior Deputy Governor. In between, he spent much of his career doing senior positions in what is now called the Canadian Economic Analysis Department until he was named Managing Director.

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Tiff is extremely well regarded by the community of central bankers and those who love them. This is reflected in his appointment as chair of the Group of Governors and Heads of Supervision at the BIS, which is the oversight body of the Basel Committee on Banking Supervision. He also is chair of the Financial Stability Board Standing Committee for the assessment of vulnerabilities. So there's a whole bunch of reasons why I've been trying, and I'm grateful to the governor and his team to make it work, trying to get Tiff to speak at Peterson for some time. But in particular, as we talk about tariffs, as we talk about uncertainty, as we talk about capital flows, as we talk about decentering of the US dollar, as we did this morning, arguably no country outside the US is more affected by all that than Canada, our most integrated partner, where there has been until just lately no real economic border and not much of another border. And, you know, there were famous economic papers written about how deep

is the border that came up in a world like Canada and US of integration. And this is a very big challenge.

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And obviously, the Bank of Canada only has to directly address part of that challenge, but they have to understand as well as possible all of that challenge and try to share that understanding with others. And so, in that— in particular in Canada, but also here in Washington and our global audience. So with that, I'm very grateful to Governor Tiff Macklem of the Bank of Canada to share your understanding of integration and when it doesn't go so well. Thank you.

[00:09:04.40] - Tiff Macklem

Well, good afternoon, Adam. I will say it's— It's a very good time for evidence-based analysis of international economics, and nobody does it better than the Peterson Institute. So it is a real pleasure to be here. I want to discuss, I'm going to make a few opening remarks, and we're going to have a nice chat. And I really want to focus on how international events, particularly events here in the United States, are affecting Canada. I came to Washington last year for the IMF meetings, and I gave some remarks at Wilson House, and my theme was the close integration between the Canadian and economic economies. And I boasted that our economic relationship is a global model for the mutual benefits of open trade and investment. What a difference a year makes. 2025 has brought radical change in our trade relationship with the United States. And as we all grapple with shifting tariffs and uncertainty, it is important that we put our heads together, we share perspectives, and I'm very much looking forward to this discussion as well as numerous discussions this week in Washington. Before I get to our conversation, I do want to highlight some of the big trends in global trade and capital flows over the past two decades.

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President Trump didn't cause these trends, but his policies will accelerate some of them and alter others. Then I'm going to touch on what this means for the Canadian economy, how the Bank of Canada is responding, and what Canada can do in the face of this global upheaval. So let me start with the four big trends. First, global trade growth has slowed. The expansion of trade after Bretton Woods began to slow around 2010, And trade barriers have been rising for the last dozen years. And now the US swerve to protectionism has increased US tariffs to their highest level since the 1930s. Second, while the US dominated global trade flows until the early 2000s, it doesn't anymore. With the ascension of China and the broadening of supply chains, global trade is now dominated by three big hubs. The United States, China, and the European

Union. But third, the US still dominates global financial flows. Now the question many global investors are asking is whether that dominance will ebb as the US pulls back from trade and runs large fiscal deficits. Liberation Day, as it's called, shook global confidence, raising questions about the US dollar's role as a safe haven.

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Since then, the US dollar has depreciated, and gold, another safe asset, is up sharply. Look, it's far too early to tell if this is a start of something. And for now, the greenback remains dominant. And frankly, without a clear alternative, I suspect it will remain the global reserve currency for the foreseeable future. But for many, its value as a hedge in times of stress has been dented. And the final trend I wanna mention is the persistence of global imbalances, the persistent current account deficits in the United States and the large and continuing surpluses in elsewhere, especially in China and the European Union. Global imbalances narrowed after the global financial crisis, but they have started to widen again. And left unchecked, growing imbalances will increase vulnerability. Sharply higher U.S. tariffs can be expected to reduce U.S. trade further, but they are unlikely to meaningfully cut the U.S. trade deficit. Yes, tariffs will reduce imports, but they will also restrain exports. Globally, U.S. tariffs, combined with the unpredictability of U.S. policy, are increasing uncertainty, they're weakening demand, and they're reducing the efficiency of global supply. Global economic growth has been more resilient to US tariffs than many expected, but we are now starting to see the impacts.

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For Canada, most goods actually continue to cross the Canada-US border tariff-free, but targeted goods face steep new tariffs, particularly steel, aluminum, automobiles, steel, and lumber. And that is having a very clear impact on our Canadian economy. In the second quarter, exports, total exports were down 27% and GDP contracted by 1.6%. Employment has also declined with job losses concentrated in those heavily tariffed sectors and related businesses. We, we do expect growth to resume in the second half of the year, but with weakness in business investment and exports and uncertainty about jobs, GDP growth is likely to be soft. Now, unfortunately, monetary policy cannot undo the damage of tariffs. Increased trade friction with the United States means our economy will work less efficiently., and there'll be added costs, and there's going to be less income. At best, monetary policy can help smooth the adjustment of the economy while ensuring inflation remains well controlled. With both— with both demand and supply impacts of U.S. tariffs and uncertainty, we are proceeding carefully. After holding the policy rate unchanged in June and July, we lowered our policy rate a further 25 basis points in September to 2.5%. Now, while monetary policy can't offset the negative effects of tariffs, positive structural reform could.

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To increase incomes and standards of living, we need to improve our productivity and competitiveness. We could have done this without US tariffs, but the loss of incomes and growth now makes this all the more imperative. And governments across Canada are rising to the challenge. There are some things that could be done quickly, at little cost, if we have the determination. Efforts are underway to reduce interprovincial trade barriers and streamline regulatory approvals. Then there are other things that require investment, and that, that'll, they'll take time to build. Here I would include better east-west transportation links to grow our internal market, and get our products to overseas markets. I'd also include new port capacity to reduce our dependence on the United States. The essential role of monetary policy is to provide confidence. The Bank cannot reduce trade uncertainty, but we will ensure that Canadians can remain confident in price stability. And with that, Adam, let's start the conversation.

[00:16:34.52] - Adam S. Posen

Thank you, Governor Macklem, for such a clear-eyed, blunt, appropriately humble and self-limiting, from the bank's point of view, opening. And some of those numbers you tossed around were pretty scary. Let's sort of start, if we could, with where you and I grew up, you much more than me, classical monetary policy, as it were. You gave a speech recently talking about the viability of the inflation targeting framework. Even under these circumstances. Can you say a bit more about how, when you are setting monetary policy and to whatever degree you're providing forward guidance, how do you take into account and respond to this U.S.-generated uncertainty? I mean, is it better that you just keep adjusting policy to the U.S.? Is it better that you try to guide some kind of expectations? I mean, these are hard choices. How are you and your colleagues your colleagues thinking about this as a strategy issue?

[00:17:48.54] - Tiff Macklem

Right.

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Since the tariff threat—

[00:17:52.35] - Adam S. Posen

Sorry, hold on. Is your mic working? If not, I'll give you mine.

[00:17:58.13] - Tiff Macklem

There we go. OK, that's better.

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Since the tariff threat started, we have been facing an unusual amount of uncertainty.

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And we've thought about this in two levels. A lot of uncertainty about US trade policy itself. Starting in about February, we had threats of universal tariffs, then we had them, then they were pulled back, we had them again, they were pulled back.

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Things have started to settle, but every week there are new events, so we'll see. What tariffs are, as those numbers illustrate, have a very material impact on the Canadian economy. So to deal with that first level of uncertainty, we've been using scenarios.

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And in particular, quite unusually, we have not published a baseline forecast since January. In April, we published two scenarios.

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That was probably the height of the tariff chaos.

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We published two scenarios, one with significant universal tariffs on Canada, a second one with pretty modest targeted tariffs. And I can tell you, even as we were deliberating, news was coming out and we were, where are we between scenario 1 and 2?

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It was a moving target.

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And then in July, we published 3 scenarios. One we called the current tariff scenario, so that basically assumed that the tariffs that were in place as of mid-July were permanent.

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And then we had a de-escalation scenario and an escalation scenario.

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And I would say that I think it's been important as part of our transparency to show to Canadians what these different scenarios could look like. It's also been very helpful for our deliberations because we've been trying to think about, OK, well, clearly, we can't really assign probabilities to these scenarios.

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So as you think about policy, You want to think about something that's reasonably robust to a range of scenarios. Then the second layer of uncertainty is, well, let's say you knew exactly what the tariffs were going to be. There's still a lot of uncertainty about what their impact will be on the economy.

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We have not had an increase in tariffs on this scale in our lifetimes.

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We do have some targeted examples, particularly in Trump One, there were some tariffs. But these are much more significant.

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And as you would appreciate, there's a lot of different elasticities.

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If the price goes up in stuff we're exporting to the United States, how do buyers in the United States respond? How substitutable is it? How much do they need the stuff?

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So there are a lot of things that we don't have very good estimates of.

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So to try to deal with that, I mean, to some extent, really, time will cure that one. You'll get the information.

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But to try to get the information as quickly as possible, we increased our—

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we do surveys of businesses and consumers.

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So, we added a lot of extra questions, particularly to businesses.

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How are you going to respond? What are you going to do with your prices? What are you doing with your suppliers, your employment plans, your investment plans?

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So, that has given us—

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good insight into how businesses are thinking about it. Since then, uncertainty about the tariffs themselves has come down, and I would say in Canada that the focus is really shifting as what happens to the Canada-US-Mexico trade agreement. And in terms of the impacts, I mean, we can get into this a bit more, but I mean, we are, As those numbers illustrated, we are seeing the impacts, and that's giving us some information.

[00:21:49.58] - Adam S. Posen

It's very interesting when— because obviously this is a challenge for all of us, but particularly for forward-looking policymakers like you and the monetary policy committees and central banks. When you're making these scenarios, how complex do you make them? The main thing, the

difference between high-low current tariffs, or do you also put in possibilities of changes in investment flows or currency, or is it you just shock the model with the tariffs? I mean, I don't want to make this sound too mechanistic, but there are, as you said, there's USMCA and that has direct effects on investment behaviors. I mean, how do you decide where to draw the line on it? How much uncertainty to consider?

[00:22:42.32] - Tiff Macklem

Well, mechanically, how do we do this?

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So we have a trade model that's more of a static multi-sector trade model that kind of anchors the fact that— I mean, we used to be on this growth path. Now there's more friction at the border.

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We're now on a lower growth path.

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And that's the part that monetary policy can't change. Then use more your dynamic models to model the adjustment from one path to the other path. In terms of the scenarios, how realistic to make them, we certainly tried to anchor them in things that the US administration were saying.

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But you don't want to spend too much time on every detail.

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You want them to be somewhat stylized, partly because the details keep changing, and partly just because you don't want people to focus too much on the decimal points. These are designed to be indicative of the broad quantum and the timing of— different scenarios.

[00:23:56.54] - Adam S. Posen

Thank you. As you and your colleagues have been assessing the impact so far, um, have there been any persistent real surprises in terms of sectoral impact, in terms of services versus goods, or traded versus non-traded, or have things been, broadly speaking, adjustments have

been more in the sectors you would have expected? I mean, again, it's, it's not so much a criticism of anybody's modeling. Our colleagues Marcus Noland and Warwick McKibbin, as kindly referenced, did some analyses trying to use a multi-sector model. But, um, just sort of more broadly, what has been the surprises, if any, and the impact on Canada so Yeah, I'll answer that in two parts.

[00:24:49.58] - Tiff Macklem

I'll answer what we predicted has more or less come out, and then the things that I think we've learned and surprised us a bit along the way. So I would say generally, talking to my colleagues in other countries, overall, the global economy has been more resilient than most people thought.

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I think Canada is a place where you can see the impacts quite clearly.

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And I mean, we were not surprised by the contraction in the second quarter. We actually had monitored a contraction of 1.5%. It came in at -1.6%. That's pretty good. Yeah, there's a bit of luck in that.

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But yes, but I mean, the idea that there would be a significant contraction I mean, we saw, as in many countries, but everything, given how integrated Canada and the United States are, I mean, you have to remember, 25% of our GDP is exports to the United States. It's a very big part of our economy. So like everybody else, we saw a lot of front-loading in the first quarter as businesses tried to get ahead of the tariffs.

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That boosted first-quarter GDP. That unwound forcefully in the second quarter, giving us a big drop in exports. And that pulled GDP negative.

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Going forward, we think GDP growth will probably be about 1%.

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So, you know—

[00:26:15.57] - Adam S. Posen

Where were we? Sorry, where was pre-crisis trend, do you think? I mean, not crisis, pre-terrorist trend was 1%?

[00:26:23.35] - Tiff Macklem

Oh, pre-crisis trend, we were growing around 2%. So, I mean, maybe—

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We've also had big swings in immigration, so that—

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that affects your potential growth. We were above 2% when we had very high immigration, maybe a little below afterwards. So we did expect to see some significant effects, and we're seeing them. And they are concentrated in the sectors that are heavily tariffed and related businesses. So the transportation business that moves steel and aluminum They're very affected. So it affects some services as well as the goods.

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I would say one thing we've learned, and it's not something that's terribly well captured in our models, is that it's not just tariffs. See, unlike if you're sitting in Europe or Japan, I think it's different than if you're sitting in Canada. Just look at a map. Canada and the United States, they're right on top of each other. There's been zero tariffs on most goods and services in Canada and the United States for a long time. Businesses have completely optimized how they do business across borders. So now you thicken that border all of a sudden, and that's a fundamental change for many businesses.

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So many businesses are looking for new suppliers.

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They're looking for new markets. That has costs. To give you a practical example, some of the goods that we import from China come through the Port of LA. Well, now, if they come through the Port of LA into the US, they face US tariffs on China before they come to Canada. So you need a new ship that comes directly to Canada.

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Those things have costs. So I think what we're hearing from businesses is it's not just the cost of a tariff.

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It's the cost of the disruption to their optimized supply chains and markets. And somebody's got to pay for that cost.

[00:28:42.56] - Adam S. Posen

We've been talking about that a lot over the last couple of weeks at Peterson events, various talks a number of us have given, the idea that— Even with— in places where there weren't such low borders, supply chains evolved organically across decades and unwinding and figuring out how to— for businesses, where to substitute, where to move, what to get in and out of is non-trivial. I mean, it's a cost and that's part of the reason potentially the inflation has been slower to appear. In the US because those decisions are still being made. Um, so stepping back a little bit from the tariffs, just thinking about uncertainty more broadly, there has been recurrent discussion through the years about the idea that partly due to global warming, geopolitics, other things, and now US actions, we're in a more shock-prone world. That we're going to get more frequent, what central bankers would call shocks, and that they may be uncorrelated but look correlated, like you get a bunch of price shocks in a row even though it's not inflation per se. Um, how has your thinking evolved on how monetary policy should respond to that?

[00:30:10.48] - Tiff Macklem

Yes, that is something we've been thinking a lot about.

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And I use that term myself quite a bit, a more shock-prone world. I've been doing monetary policy for a long time. And I won't say that it felt easy at the time.

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But at least in principle, in a world that's dominated by demand shocks with some temporary supply shocks, monetary policy in principle is pretty straightforward. Right.

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It's always more complicated in the moment.

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But in principle, well, you lean against the demand shocks.

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Look through the supply shocks. I think what we learned in COVID is that not all supply shocks are that temporary.

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They can be pretty persistent.

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You can have multiple supply shocks accumulate.

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So even if each one is not that long-lasting, the accumulation is quite material. And the other thing we learned in—

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COVID is that the state of the economy matters a lot for the inflation outcome.

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And we haven't had very many periods where we got a negative supply shock at a time the economy was overheated.

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It just hasn't happened much in the last 30 years. But coming out of COVID you had really strong demand with supply that was still quite constrained.

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And that, I think—

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so we got an outsized burst of inflation as a result.

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And there are a lot of papers that very interestingly separate, OK, was this mostly a demand shock or mostly a supply shock? But I think once you realize that the sort of state of demand versus supply matters for the outcome, separating them actually becomes less useful than it used to be.

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So, I mean, one thing, certainly one of my takeaways is that if you get hit with a negative supply shock and your economy's in excess demand, that can cause a lot more inflation.

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And what we really saw was we saw the pricing behavior of firms change quite starkly during COVID. They were both increasing their prices in bigger steps, and they were taking those steps more frequently.

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And that's how you get from like 2% to 8% inflation pretty quickly. So, I mean, coming back to your question, yes, there are, I would agree.

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I think we've got wars, we've got geopolitical fragmentation, we've got tariffs, We've got demographics. In principle, demographics is a fairly slow-moving thing. But the US, you've cut immigration sharply. Even in Canada, there was basically no immigration for obvious reasons during COVID. Then we tried to make up for the lack of immigration post-COVID with a big increase in immigration.

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We overdid it.

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And now we've pulled it back down quite low.

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And immigration has been a big part of our economy. That is having more of a supply-side effect. So I think my takeaway is, and the phrase I've been using is, we need a richer playbook for supply shocks.

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I don't think we can just say, oh, supply shock, look through that.

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I think it's more context-specific to what's the state of the economy when the supply shock hits. Are we in excess demand? Are we in excess supply? That's going to matter, I think, to your response to the supply shock.

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And then some assessment— of course, you'll never know for sure—

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but some assessment of how persistent this might be. So that is something we actually, as you probably know, we do review our inflation or our monetary policy framework every 5 years. The next review, it needs to be renewed next year. So, we've identified a number of questions to look at in the context of that review, and that is one of them. One thing in Canada is we have a 2% inflation target, and we also have inflation, a band of 1 to 3%, which is really designed to give people an idea of, okay, well, this is not literally going to hit 2, but if it's between 1 and 3, it's kind of normal. We do have a flexible inflation targeting.

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Framework.

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So, you know, do we have scope to use that flexibility in the face of supply shocks? I think that's something we're thinking about. And how would you use it?

[00:34:49.02] - Adam S. Posen

Delighted to hear you're including these questions in your framework review. I'll be very excited to read it. I'm hoping in our global audience—

[00:34:59.58] - Tiff Macklem

Yeah, send me your thinking.

[00:35:01.55] - Adam S. Posen

Yeah, there are a few people who will also be excited and tracking now Bank of Canada's Strategic framework review. Let me ask one more question, if I may, before I open it up to our in-person audience. So you mentioned the list of supply shocks. As our colleague Karen Dynan discussed last week in our Global Economic Prospects, there is a very big driver of potentially persistent driver of US growth and inflation coming out of AI investment. There are also seemingly quite persistent moves in US fiscal policy. We tend to talk about this in the framework of R-star goes up in the US as capital returns go up and fiscal, sustained fiscal demands go up. Canada, this is more of a question, not a statement, but Canada, I don't think has the same kind of AI investment boom that we do.

[00:36:14.22] - Tiff Macklem

I don't think anybody does.

[00:36:16.23] - Adam S. Posen

I don't think anybody does, for good and for ill. And also Canada, mostly for good, I don't think has had the kind of fiscal erosion. That post-COVID that the US has had and in prospect. Is it useful to think about r-star diverging between the US and Canada, and how do you think that matters if it does? I mean, it's obviously not observable, but as a concept.

[00:36:48.38] - Tiff Macklem

Yes. Well, I do need to start with that.

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It's not observable. It's a great concept.

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You need an estimate of r -star in your model.

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We're transparent about our estimates of r -star. We publish them. But one monetary policy decision to the next, it's not that useful. I will— to your question, I mean, it is a question.

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It's another question we're starting to ask ourselves. So, you know, just mechanically, we update our estimates of R -star and potential output once a year. Obviously, they're somewhat interlinked.

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And we publish those as an annex to our monetary policy report each April.

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So, we will be, you know, we will be getting to that. You know, that work is underway. And as we get towards April, we'll take those decisions. Certainly, for as long as I can remember, our estimates of R -star in Canada and the United States have been the same. And that really just reflects the fact our economies are so integrated. There's very little friction at the border. Why would they be that different? And the exchange rate, if they were fundamentally different, you'd think they would have more of an exchange rate consequence that we haven't seen.

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Historically, we do model them separately, and they typically come out—

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I'm not saying the estimates are exactly the same, but they're close enough that we set them the same. But yes, I think we have started to ask ourselves that question. Could they be getting different? For exactly the reasons you suggested. I mean, US productivity growth, even without AI, has been running well ahead of Canadian productivity growth. If AI is going to boost US

productivity growth further, still an open question, but there's certainly potential for that to happen.

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Add in the term premium could go up with large ongoing US fiscal deficits.

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Yes, I think, you know, R-star in the United States could be above our R-star in Canada.

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So yeah, we'll do the analysis. We'll come to a conclusion.

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There's no guarantee the conclusion's going to be right, because we can't observe R-star in the US or R-star in Canada. But we'll have to come to our best judgment.

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I will say, from a monetary policy perspective, of the things I worry about, I don't lie awake at night worrying that we got R-star wrong.

[00:39:36.08] - Adam S. Posen

Right.

[00:39:36.50] - Tiff Macklem

Because if R-star is wrong— I mean, R-star, if it changes, it probably changes kind of gradually over time. And so if we have it wrong, we'll start to see our inflation forecast keeps coming either too high or too low.

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And we'll revise. And it's sort of the beauty of inflation targeting.

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I mean, yeah, you're going to make some mistakes, but the idea is to make small mistakes and just keep aiming back to your target. So yeah, if inflation keeps coming in too high, we're going to raise rates and get it back down.

[00:40:16.07] - Adam S. Posen

Sounds right. Let me open it up to questions from the audience. Jessica in front has a roving mic. I think Patrick's up first. Jessica, and those in the back can stand at the standing mic. Please ask a question, don't make a speech, and please identify yourself. Thanks very much.

[00:40:40.19] - Audience

I'm Patrick Honohan from Peterson Institute. My question is about international central bank cooperation. I mean, your position as chair of the oversight body on the Basel Committee, it gives you a great viewpoint on that. In the context of this geopolitical fragmentation, do you see central bank cooperation continuing as strongly into the future as before, or do you worry a bit about an erosion of the quality of that cooperation on things like banking supervision but also other aspects?

[00:41:12.37] - Tiff Macklem

Um, well, I, I do worry more generally about fragmentation and lack of cooperation. The reality is international cooperation's never been completely straightforward. It's never really been easy. But there are so many issues. As our economies all become more integrated, there's so many things that we can't deal with by ourselves. We need to cooperate. Financial stability is a great— A great example. Climate change, another example. Trade, obviously. So we do need international cooperation. With respect to central banks, I mean, the good news is central banks are not political institutions. They're very evidence-based. They're run by technocrats. So actually, I— I think I meet with my governor colleagues regularly in Basel at the Bank for International Settlements. We're all here this weekend. We meet at the IMF, the G20, the G7. So, you know, we do meet regularly. We have candid conversations. We exchange information. And, you know, our mandates are each for our domestic economies. And that grounds us. But we can all see that there are many things if we work together on, every one of us is going to be better off.

[00:42:49.24] - Adam S. Posen

Another question from the audience, please, over here.

[00:42:56.29] - Audience

Hi, Robert Martin, Millennium. I just had a question. We were talking about r^* , right, and that slowly evolving. R-star in this situation where you have these really sudden, really big changes, right? We talked about— you talked about immigration affecting potential, clearly tariffs, same, et cetera. When you get these sudden shocks, do you worry that maybe in this environment, R-star can shift structurally and fundamentally faster than we're used to? It's a good question.

[00:43:28.07] - Tiff Macklem

Yes, I mean, I think it could. And if you look at—

[00:43:33.40]

to your point, if you look at actual empirical estimates of r^* , you do see some periods where they seem to have declined. I mean, if you look around the global financial crisis, most estimates of r^* go down fairly quickly, and then they're low, and then seem to be coming up a bit. So yes, maybe it's not quite as gradual as— there is risk that it's not super gradual.

[00:44:03.53]

I still think that flexible inflation targeting is well-equipped to deal with things that don't change too quickly because you just keep your eye on the target. If something changed so you're missing it, well, you just—

[00:44:23.13]

you adjust and you're committed to getting back to target. But yes, when things change quickly, given that there are lags in monetary policy, yeah, it's more complicated.

[00:44:37.46] - Adam S. Posen

Back, Mike.

[00:44:39.25] - Jacob Funk Kirkegaard

Jacob Kirkegaard from the Peterson Institute. Well, thank you for a set of very interesting remarks. I got one specific question that pertains to tariffs. Tariff revenues and general uncertainty. I mean, there are many people here at the Peterson Institute who have been trying to gauge different metrics for what is the actual level of tariffs implemented and tariff revenue collected. And one of the seemingly sources of variation or uncertainty, if you like, is the share

of US-Canada trade covered by USMCA and thus not subject to tariffs, as opposed to There has been a very large seeming shift recently in that share. Can you share some light about the magnitudes of that, the drivers of it, and of course, preferably, the future of it? Thank you.

[00:45:31.43] - Tiff Macklem

OK, well, the future is always harder than the past. But yes, I can shed a bit of light on it. And I'd be very interested in seeing whatever work you can share because, yes, we're looking at all the same things you're looking at. The average tariff rate versus the tariff revenue, and there's, as you said, there's a pretty big gap. So in Canada, outside of the targeted tariff areas, steel, aluminum, autos, lumber, if you are USMCA compliant, so that's the US, Canada, Mexico, we actually like to call it CUSMA, the Canadian-US-Mexico Trade Agreement. But I'm in the US, so I'll call it USMCA. If you're compliant with that, you're tariff-free. So before— and if you're not compliant with that, there's a 35% tariff. So there's a very high value of being compliant. So before President Trump put in place the 35% tariff if you're not CUSMA compliant, the average tariff rate was about 2.5%. So for many companies— and if you want to be CUSMA compliant or USMCA compliant, you need an audit trail. You need to bring the auditors in. You've got to make sure all your parts are coming from Canada, US, or Mexico.

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You've got to validate that. So there's some cost. And there's a bit of lack of flexibility if you need a part from another country. So many companies— before didn't bother. So it was somewhere in the '60s that were 60-something percent were compliant. It's now up to 95%. So they've brought in the auditors, they're tracking their supply chain, because the cost of not being is very significant.

[00:47:23.14] - Adam S. Posen

Thank you. I think we have time for one more question before the governor has a hard stop. If there is no one, I will pose it. Um, sort of going back on a few things, including your response to Patrick on cooperation, and with your BIS chair hat on, um, there is another potential of many sources of divergence that the ECB, the People's Bank of China, the Bank of England are pursuing, um, uh, central bank digital currencies. Um, the U.S., thanks to the Genius Act, um, is not allowed— doesn't allow the Fed to even research a digital currency. Um, but the Trump Treasury is very committed to promoting stablecoin use tied to short U.S. Treasury bills. Again, in terms of sort of central bank cooperation, and more importantly, since central bank cooperation is just a means to an end, in terms of financial stability, is this neutral? Is this

something you're concerned by? Are there discussions amongst the central bank community on how to navigate this divergence?

[00:48:49.48] - Tiff Macklem

Look, it's a very good question. And I think, particularly with respect to stablecoins, I think, well, there's benefits and there's risks.

[00:49:02.40]

And you've got to look at both sides. Stablecoins, to this point, have not really been used in a significant way as a means of payment.

[00:49:11.56] - Adam S. Posen

Right.

[00:49:12.25] - Tiff Macklem

They've been used largely as an intermediate between different crypto assets.

[00:49:20.13]

If they become a means of payment— and certainly the Genius Act lays down a legislative framework to support that— the key thing is they need to have a fixed value with your fiat currency. Andrew Bailey often used the term singleness of money. And so the risk is if that gets called into question, you get a run, like you get a deposit run. I mean, that's a fundamental sort of feature of central money, private sector money, and not central bank money.

[00:50:06.05]

And the Genius Act, I think, provides legislative framework.

[00:50:08.43]

They've got to be fully backed with with very high-quality assets, relatively short-term, can't pay interest.

[00:50:17.08]

So yes, I think in the design, in Canada, Europe is moving forward.

[00:50:23.41]

Canada, we are in the process of— it's really the finance department. The government is looking at this, and they're working on it. But yes, you want to make sure you design it so that you get you get the benefits without the problems. The benefits, I mean, I think it will be very interesting just to see how big is the adoption, how big is the space for stablecoins. I think there are clearly some parts of the system that are not well served. They're not very efficient. Cross-border payments would be probably the most obvious example. They're slow, clunky, and expensive. And stablecoins could speed that up at much lower cost. So there certainly are some applications. We'll see how broad-based they are. With respect more broadly to CBDC, at the Bank of Canada, we've done a lot of work on central bank digital currency.

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Whether we have one or not in the country is not a decision for the Bank of Canada.

[00:51:32.11]

It's a decision for the government. There doesn't seem to be a really strong demand on the part of Canadians to hold central bank money in a digital format.

[00:51:42.34]

There are many—

[00:51:43.22]

Canadians have many ways to make digital payments. They're pretty well served. So, at this point, we're ready to go if the decision is that's something Canada wants to move forward on. But at this point, we've kind of parked that.

[00:52:01.49] - Adam S. Posen

Great, thank you. With that, we're going to close. I just want to remind everyone watching online and here today that our macro-focused events continue here at the Peterson Institute. Tomorrow morning, we'll have a number of TIF's colleagues: Agnès Benassi-Quéré, Klaas Nolte, Signe Kronstrup, Olli Rehn, and our former fellow Angelo Bide. Talking about Europe in a changing international monetary system. We may ask some of the same questions we asked Tiff. But also in roughly 2 weeks, on October 29th, we'll be having Senators Rand Paul and Tim

Kaine talking about a bipartisan conversation on Congress's role in the trade war, which might someday have implications for Canada and the world. And finally, in 2 weeks from Friday, 2 weeks from tomorrow, we'll be having a high-level conference on central bank independence and practice, and included among the distinguished speakers is Tiff's former colleague Carolyn Wilkins on the issues of central bank accountability. So with that, please join me in thanking Governor Tiff Macklem of the Bank of Canada.