Daily Economic Update

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US midterm election results as expected — limited impact on Canadian outlook

A mostly as-expected outcome from the U.S. midterms — the Democrats retaking the House but Republicans adding modestly to their majority in the Senate — does not have a significant impact on our outlook for the U.S. or Canada. The main risks in terms of the Canadian economic outlook are what happens to U.S. trade policy — particularly the prospects for the passage of the USMCA and the end of existing 'Section 232' steel and aluminum tariffs — and any changes to the U.S. fiscal policy stance.

USMCA probably still on track: The new NAFTA replacement, the 'USMCA', is still likely to be approved by Congress. The Democrats will want to avoid handing the Trump administration political "wins" but will also probably find it difficult to oppose some of the changes in the deal versus NAFTA, including the high-wage requirements in the auto sector. Of course, the agreement will ultimately also need to be ratified by Canada and Mexico but we continue to think the most likely outcome is the deal will move forward. None of the three trade partners will want to reopen an acrimonious debate that contributed to increased uncertainty for businesses and less investment in all three countries. NAFTA remains in effect in the mean-time.

Pushback on presidential 'Section 232' powers? The President has used dubious national defense (section 232) arguments to justify imposing tariffs on steel and aluminum products primarily on close allies including Canada. Canada already obtained some protection from future measures in the new USMCA. Traditionally more protectionist democrats perhaps won't see reducing trade barriers as a key top priority but could presumably kick up more resistance to what is arguably a misuse of presidential authority. Tariffs used in the escalating trade spat with China have for the most part not made use of section 232 measures.

How long can fiscal tailwinds blow? The combination of US tax cuts and spending saw the U.S. government budget deficit balloon to $800 billion in 2018 (about 4% of GDP) under the current administration. That is providing a significant tailwind to economic growth, some of which — particularly stronger growth in the industrial sector — is spilling over into Canada. With the split Congress, political gridlock is a risk and additional tax cuts are much less likely. There may yet be room for a compromise on spending plans, though.

Nathan Janzen | Senior Economist | (416) 974-0579 | nathan.janzen@rbc.com
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