ECONOMIC VIEWPOINT

Shifting Gears: Ontario's Manufacturing Sector amid Tariff Turmoil

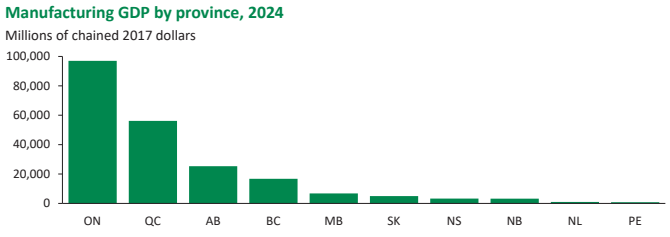
By Florence Jean-Jacobs, Principal Economist

- National manufacturing powerhouse Ontario is particularly exposed to shifting US tariff announcements and the attendant uncertainty. The automotive and primary metal manufacturing sectors are particularly exposed, but ripple effects are expected in the broader business ecosystem.
- The auto sector is capital intensive and regionally concentrated, making it vulnerable to prolonged tariffs. Amid tariff uncertainty and reduced demand, some automakers have already announced temporary shutdowns and layoffs at assembly plants in the province. Additional job losses are expected in the coming months.
- While the current trade environment poses significant challenges, modernization and diversification offer long-term opportunities. Greater adoption of advanced manufacturing technologies shows promise and could enhance Canada's current lacklustre productivity picture. All else being equal, increasing annual labour productivity growth by 1 percentage point in Ontario's manufacturing industry would boost overall business sector productivity growth in Canada by 0.06 percentage points.
- Boosting interprovincial trade and diversifying export markets can build resilience, but progress has been uneven across sectors and moderate over time. Encouraging examples include the computer and electronics and aerospace sectors, which have achieved a more internationally diverse customer base.
- Even with the right policies, the trade and economic transition will not be painless for Ontario, as diversification is a long-term endeavour and productive capacity cannot be quickly reallocated without some labour and capital losses.

Introduction

In a context of constantly shifting tariff announcements coming from the US administration, Canadian manufacturers are understandably struggling to find a solid footing, and some are already pausing projects and major investments. Given the highly volatile environment expected in the next four years, the question becomes how to navigate this uncertainty and the major shift in the international trade paradigm. In this Economic Viewpoint, we analyze the current state of Ontario's manufacturing industry, with a focus on sectors that are more vulnerable in the face of US tariffs. We then lay out some of the levers and opportunities ahead at this time of transformation.

Graph 1
Ontario Is Canada's Manufacturing Powerhouse



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The author would like to thank manufacturing industry experts at Next Generation Manufacturing Canada (NGen) for their generous comments and insights.

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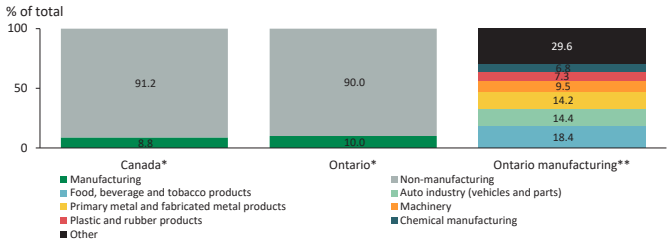
Why Manufacturing Matters for Ontario

Ontario is Canada's manufacturing powerhouse, with manufacturing output that is well ahead of other provinces' (graph 1 on page 1). One in ten jobs in the province is in manufacturing, above the national average (graph 2). And while the auto industry is a major employer, the largest share of manufacturing employment in 2024 was in food and beverage production. In fact, four key manufacturing sub-sectors are fairly evenly split in terms of their contribution to GDP in the province: autos, chemicals, food and beverages, and metals (graph 3). In the last decade, the share of chemical and food and beverage manufacturing has expanded. Meanwhile, the auto industry saw its relative share decline from 18.8% to 15.9%.

Graph 2

One out of Ten Jobs in Ontario Is in the Manufacturing Industry

Employment by sector, 2024



* Labour Force Survey. ** Survey of Employment, Payrolls and Hours.
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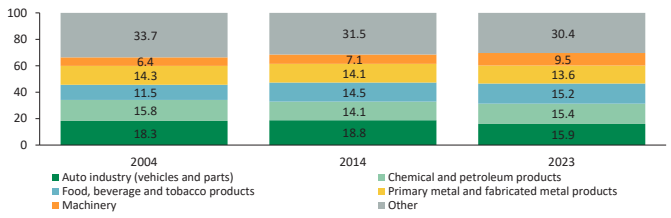
Graph 3

Autos, Chemicals, Food and Metals Form the Core of Ontario Manufacturing

Ontario manufacturing GDP by subsector, 2023



* Numbers may not add up to 100 due to rounding.
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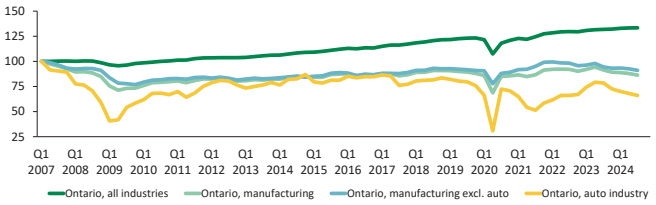
The auto industry has had its fair share of ups and downs in the last 20 years (graph 4). The industry never fully recouped its losses from the global financial crisis (GFC), and post-pandemic recovery has been modest.

The sector is particularly vulnerable in today's trade environment. It is capital intensive and concentrated both industrially (two-thirds of employment and output is in the auto parts subsector) and regionally (Southwestern Ontario) (graph 5). This makes it harder to adjust quickly to shocks: job and productive capacity losses could become lasting if tariffs persist over an extended period. Underused capacity and permanent layoffs in the auto industry would pose significant downside risks to Ontario's economic forecast. (See box 1 on page 3 on the auto industry.)

Graph 4

Manufacturing GDP Never Fully Recovered After the 2008–2009 Global Financial Crisis

Real GDP at basic prices in chained 2017 dollars, Ontario, Q1 2007–Q3 2024



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Graph 5

Nearly One in Five Jobs in Windsor Is in Manufacturing

Manufacturing employment by Ontario CMA,* 2024

* Census Metropolitan Area.
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Which Manufacturing Sectors Are Most at Risk in Ontario?

Given the share of domestic output that is directly exported to the US, the automotive and primary metal manufacturing sectors are most vulnerable to a trade war (graph 6 on page 3). Two-thirds of auto revenues come from exports to the US, and that share is 50% for primary metal products (iron, steel, aluminum and non-ferrous metals)—a fair share of which is further transformed to be integrated in vehicle components. Other subsectors warrant monitoring, with a third or more of production directly dependent on US demand: miscellaneous manufacturing, industrial machinery, pulp and paper, plastics, wood and chemical products. Drilling down further, we see that several high-value-added subsectors even exceed 50% US exposure (table 1 on page 3). Steel producers also face a very challenging situation: those that export directly to the US now face a 25% tariff, and those that supply the Canadian auto industry and other domestic manufacturers anticipate a major slowdown in demand due to reduced export demand. Moreover, contrary to aluminum, for which US businesses have few alternatives to importing the resource, Canadian steel manufacturers face tougher competition from US producers themselves in what is currently a fairly well-supplied global and

Box 1: Tariffs Are Wreaking Havoc on Auto Industry Supply Chains

At the time of writing, motor vehicles were subject to 25% import tariffs in the US that went into effect April 3. (See table 2 on page 4 for a list of effective and upcoming US tariffs facing Canada.) For Canadian exports of motor vehicles, a 25% tariff is applied to the non-US content of the vehicle, even if it is compliant with CUSMA. With regards to auto parts, a similar 25% tariff is forthcoming, although CUSMA-compliant auto parts may be exempted a little longer than those that don't fall under the agreement's purview. Auto parts that are not CUSMA compliant are expected to be tariffed at 25% sometime between now and May 3. As for CUSMA-compliant parts, a date for tariff application has not been set as of the time of writing, in part due to the complexity of identifying US vs. non-US content. This could leave further room and time for Canada to negotiate exemptions.

This means that for the time being, Canada and Mexico are still at a relative competitive advantage compared to other countries, at least as long as the CUSMA exemption holds. But with the tariff situation constantly in flux and the stated objective of the US administration to reshore auto manufacturing, Canada's auto sector is still in a vulnerable position. What is less clear is how reshoring the entire value chain and ecosystem of suppliers can be realistically accomplished, as integrated supply chains across the North American continent were decades in the making. It might require substantial new investment to increase US domestic capacity to replace Canadian supply. Still, for manufacturers with factories producing similar goods on both US and Canadian soil, we may see a greater increase in investment in US plants, to the detriment of Canadian facilities.

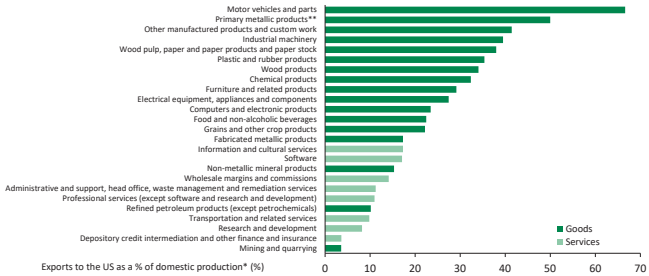
Stellantis, the maker of Chrysler and Dodge, announced a two-week pause at its Windsor assembly plant starting April 3. And on April 11, GM announced a temporary shutdown and reduced production at its CAMI assembly plant in Ingersoll due to decreased market demand. Others may follow suit amidst the prevailing uncertainty. Automotive original equipment manufacturers (OEM) present in Ontario include Ford, GM, Stellantis, Honda and Toyota.

One cause for cautious optimism is a potential agreement regarding auto parts. Most auto industry jobs in Ontario are at auto parts manufacturers, which include players like Linamar Corporation, Magna International and Martinrea International. If CUSMA-compliant auto parts remain exempt from tariffs, this would limit disruptions, since many of these parts are difficult to substitute and are almost entirely produced in Canada or Mexico. Still, uncertainty and changing demand from automakers will probably keep these players on the sidelines, limiting hiring and investments. And there is no guarantee that parts won't eventually get hit by tariffs later in the year.

Graph 6

Ontario's Auto Sector and Primary Metal Manufacturers Are Most Exposed

Share of Ontario domestic production that is exported to the US, as a % (top 25 subsectors*)



* 2021 data. Industries shown: Ontario's top 25 industries that export to the United States (3-digit NAICS codes, with some exceptions to carve out the auto sector).
Formula: Domestic exports from Ontario to the United States as a percentage of domestic production. Services were estimated using Canadian data. ** Excludes scrap metals.
Statistics Canada input-output tables and Desjardins Economic Studies

Table 1

Five Manufacturing Subsectors Rely on the US for over 50% of Revenues

	MANUFACTURING SECTOR	NAICS CODE	ONTARIO EXPORTS TO THE US*	
			MILLIONS OF $	AS A % OF REVENUE
1	Distilleries	31214	573	85
2	Resin and synthetic fibres	3252	3,189	69
3	Motor vehicles and parts	3361, 3362, 3363	39,582	67
4	Aluminum production and processing	3313	1,484	62
5	Non-ferrous metals (excl. aluminum)	3314	12,990	51
6	Iron and steel products and foundries	3311, 3312, 3315	9,484	48
7	Bakery products	3118	3,703	47
8	Misc. manufacturing (including medical equipment and supplies)	339	5,340	41
9	Sugar and confectionery products	3113	1,125	41
10	Machinery	333	8,354	40
11	Pulp and paper products	322	3,222	38
12	Grain and oilseed milling products	3112	2,089	36
13	Plastics and rubber products	326	6,020	35
14	Wood products	321	2,706	34
15	Furniture and related product manufacturing	337	1,704	29
	MANUFACTURING	**31, 32, 33**	135,044	39

* 2021 domestic exports.

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local market. And we anticipate additional second-round effects will amplify the initial trade and uncertainty shock. Several suppliers depend on the auto industry and other manufacturers, selling them key inputs, equipment and services. Think transportation and logistics firms, for instance. It's therefore a broader business ecosystem that would experience a drop in demand as original equipment manufacturers (OEM) and Tier 1 clients pause orders and investments. This would entail ripple effects on regional job markets and, ultimately, household consumption.

What Tariffs Mean for Ontario's Labour Market

As discussed in a recent analysis, we estimate that about 7% of Ontario's jobs are directly linked to exports to the US, and about 4.5% are not only exposed to trade, but are also in vulnerable sectors (defined as sectors that risk experiencing a sharper drop in output due to reduced US demand). A striking example is the auto sector (graph 7 on page 4). Canada, including Ontario, is expected to experience a recession in 2025. If the current tariffs remain in place for the rest of the year and compliance with the Canada-US-Mexico Agreement (CUSMA)

Table 2
US Tariffs Impacting Canada

TARIFF EFFECTIVE DATE	AFFECTED PRODUCTS	TARIFF RATE	AFFECTED REGION	STATUS
March 4 and 7 *(Rationale: border/fentanyl)*	10% on energy, critical minerals[1] and potash. 25% on all other imports except CUSMA-compliant products. March 7: 0% on CUSMA-compliant products and the auto sector (for autos: exempted only until April 2).	25% and 10%	Canada, Mexico	Effective
March 12	Additional 25% tariff on aluminum and steel.[2] No CUSMA-compliant exemption.	Additional 25%	World	Effective
April 3	Additional 25% tariff on foreign-made autos. 25% on non-US content of CUSMA-compliant autos.	Additional 25%	World	Effective
April 4	25% tariff on beer made from malt (aluminum component)	Additional 25%	Canada, Mexico	Effective
May 3 and later	On or before May 3: Additional 25% on non-CUSMA-compliant auto parts. Later (date unknown): 25% tariff on non-US content of auto parts that are CUSMA-compliant.	Additional 25%	World	Upcoming
Unknown	Semiconductors, lumber, pharmaceuticals, dairy, copper	Unknown	Canada, World	Upcoming

[1] Some types of aluminum are treated as critical minerals, but not all. [2] Definition evolved to include products like canned beer (effective April 4).
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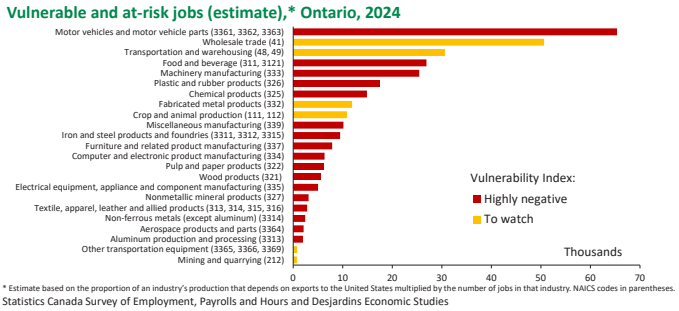
Graph 7
Some 65,000 Auto Sector Jobs Are at Risk in Ontario



* Estimate based on the proportion of an industry's production that depends on exports to the United States multiplied by the number of jobs in that industry. NAICS codes in parentheses.
Statistics Canada Survey of Employment, Payrolls and Hours and Desjardins Economic Studies

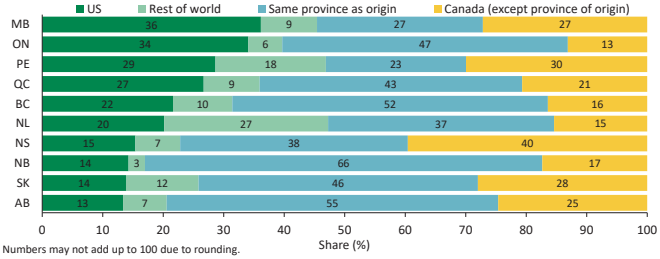
does not improve, Ontario's unemployment rate could approach 9% in late 2025 (up from 7.5% in March 2025), with some sectors likely seeing net job losses and a reduction in hours worked. We could see additional layoffs in the manufacturing sector as well as industries that depend directly and indirectly on trade: wholesale, transportation and warehousing. Crop and animal production and forestry likely won't be spared, as any shock to the manufacturing sector would have ripple effects on producers upstream. However, the situation is highly fluid, and the unemployment rate may not increase as sharply if more producers start adhering to CUSMA regulations. Additionally, the government of Ontario has announced measures to mitigate the impact, including 6-month tax deferrals, which should provide $9B in cash flow to businesses, along with a $2B rebate from the Workplace Safety and Insurance Board to support workers. Additional support may be introduced as the province tables its 2025 budget, which could help cushion the labour market from the effects of US tariffs in the near term. However, governments will be reluctant to extend support indefinitely. In an adverse scenario where tariffs and the attendant uncertainty persist over a prolonged period, disruptions to the labour market would ensue, only at a later date.

Where Do We Go from Here? How Can Manufacturers Adapt?

Boosting Interprovincial Trade and Diversifying Export Markets

Ontario's manufacturing sector is the second most US-dependent among Canada's provinces after Manitoba (graph 8). It also has the smallest share of interprovincial trade (13%), although this is in part due to the sheer size of its internal market: 47% of manufacturing shipments stay in Ontario. This has spillover benefits for the broader Ontario economy, as manufacturers supply productivity-enhancing equipment for key Ontario industries like mining, energy and agriculture.

Graph 8
Ontario's Manufacturing Sector Is the Second Most US-Dependent Among the Provinces
Share of manufacturing sales by destination, 2023



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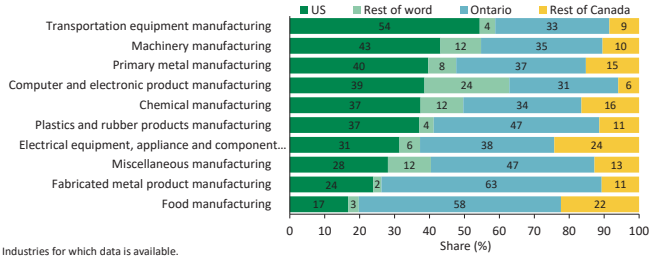
The province's US dependence is largely driven by transportation equipment manufacturing. Graph 9 shows that other subsectors have greater market diversification, both within Canada and in other countries besides the US. Food manufacturers, for instance, cater primarily to local market demand. So do fabricated metal producers, although presumably the end client could well export to the US afterwards, especially if it is an auto value chain supplier. In terms of international diversification, the clear leader is computer and electronic product manufacturing, with 24% of shipments destined to non-US overseas destinations. This is cause for optimism: global demand for Canadian manufactured products, especially leading-edge and high-tech goods, is by no means limited to our neighbour to the south. Reducing reliance

Graph 9
Ontario's US Dependence Is Largely Driven by Transportation Equipment Manufacturing
Share of Ontario manufacturing sales by destination, 2023*



* Industries for which data is available.
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on the US across other subsectors could build resilience for Ontario's manufacturing industry as a whole. But the path to that destination is by no means easy, nor is it a short-term endeavour.

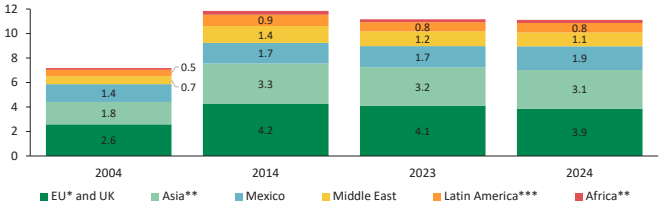
Over the past 20 years, Ontario manufacturers have only moderately diversified away from the US, turning mostly towards Europe, Asia and Mexico. Progress on diversification was made primarily between 2004 and 2014, with a deceleration in the last decade (graphs 10 and 11). The 2008–2009 GFC exposed the vulnerability of Canada's manufacturing sector to overreliance on the US, which prompted some diversification efforts, but they were ultimately limited. The current predicament could be the wake-up call needed to accelerate the diversification trend seen in the 2004–2014 period. Judging by the evolution of transportation equipment, diversification is a feasible goal, though decades in the making. For instance, it took 20 years for the Ontario aerospace sector to reach a non-US share of exports of 31.5% (up from 18.5% in 2004). In all, the road to diversification remains a difficult one. It requires established networks and often involves overcoming non-tariff barriers such as regulation, standards and cultural differences, which is why government support is invaluable for businesses engaging in that shift.

Graph 10

Ontario Manufacturers Have Diversified Away from the US Since 2004, Especially to Europe, Asia and Mexico

Ontario domestic exports of manufactured products by destination, 2004, 2014, 2023 and 2024

% of total (total includes US)



* European Union, 2024 definition. ** Excluding the Middle East. *** Excluding Mexico.
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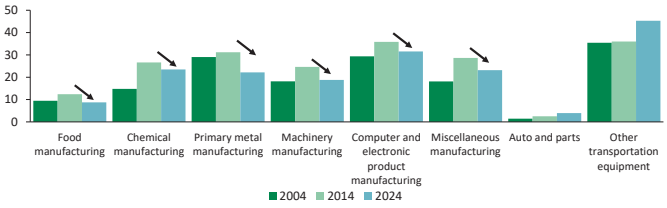
Graph 11

Diversification Wake-Up Call? Most Manufacturing Sectors Increased Their Dependence on the US Market in the Last Decade

Ontario domestic exports to countries other than the US, 2004, 2014 and 2024

% of domestic exports by industry



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Accelerating the Shift Towards Advanced Manufacturing

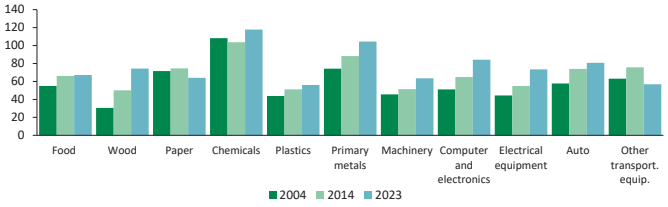
Ontario's manufacturing sector has seen a significant increase in labour productivity (real GDP per hour worked) over the last 20 years. It rose from $58 per hour worked in 2004 to $74/hour in 2023. That's a 1.2% compound average growth rate (CAGR), compared to the 0.8% average for the Canadian business sector as a whole. While chemical manufacturing maintained the highest level of labour productivity throughout the period, other sectors also saw sharp increases (graph 12). This includes wood products (+4.8% CAGR), computer and electronics and electrical equipment (both +2.7%), primary metals (+1.8%) and the auto industry (+1.8%). In contrast, labour productivity fell at paper product and other transportation equipment manufacturers.

Graph 12

Productivity Remains Highest in the Chemical Sector

Labour productivity in Ontario by manufacturing subsector, 2004, 2014 and 2023

2017 $ per hour worked



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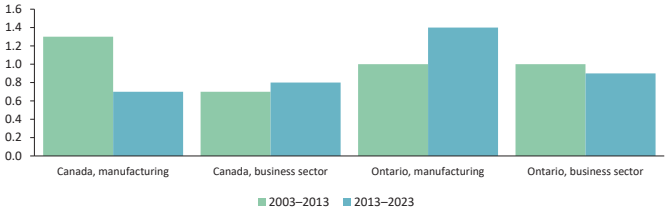
What conclusions can we draw from this? Ontario's manufacturing sector has posted above-average productivity growth in the last two decades while navigating major hurdles like the GFC and the pandemic, which upended supply chains, forced shutdowns and accelerated the transition to telework (graph 13). This performance is thanks in part to the greater adoption of advanced manufacturing technologies. And recent developments are promising. According to Canadian Manufacturing's latest outlook, manufacturers are increasingly turning to industrial internet of things (IIoT) (which allows, among other things, predictive maintenance with real-time data),

Graph 13

Productivity Growth in Ontario's Manufacturing Sector Beat the Canadian Business Average in the Last Decade

Annual average productivity growth

Compound average growth rate of labour productivity (real value added* per hour worked), %



* In chained 2017 dollars.
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automation, artificial intelligence, machine learning and cloud computing. There is also growing interest in drones and quantum computing. Advanced enterprise resource planning (ERP) systems are now commonplace. However, there is still room for improvement, with adoption of robotics lagging in sectors other than automotive (NGen, 2024). Recent ventures and funding to boost AI-powered technology such as automation and advanced materials development are steps in the right direction, showing promising results.

This is encouraging, as the commercialization and business adoption of AI has been weaker in Canada than in other major economies. (See our analysis.) And while the US may offer fewer immediate opportunities in green and sustainable technologies, companies in this sector can explore more promising opportunities in Europe, where investments and interest in renewable energy remain strong. Major investments in energy infrastructure and defence in Europe are also generating opportunities for Canadian manufacturers. If carefully calibrated, Canada's commitment to reaching the 2% of GDP NATO target for defence spending should also generate defence procurement contracts that could benefit homegrown manufacturers.

Ready for the Rebound

Despite these positive opportunities, firms are rightfully concerned about making major investments in today's uncertain trade environment. Boosting production or making expansion plans could be risky when revenue streams are less than secure. But businesses should keep in mind that modernization will continue to be a differentiating factor in order to compete in the new economic reality that emerges after this economic storm. Laying the foundations for enhanced productivity today through innovation and technology integration will position Canadian manufacturers advantageously in the long term. And Ontario has a major role to play in improving Canada's productivity picture as it represents 6% of the Canadian business sector value added. All else being equal, increasing annual labour productivity growth by 1 percentage point in Ontario's manufacturing industry would boost overall business sector productivity growth in Canada by 0.06 percentage points.

Conclusion

The current trade environment will inevitably cause some difficult reshuffling of factors of production in Ontario's economy in 2025 and 2026, and job losses appear unavoidable. We expect the auto sector to struggle most given its integrated value chains with the US and high dependence on this export market. Primary metal manufacturers are also vulnerable, and second-round effects are expected in the broader economy. The current context may be the wake-up call needed to renew the impetus to accelerate interprovincial trade, diversify exports and boost ongoing modernization through technology integration and innovation. Carefully crafted policies to accelerate automation and market diversification across the value chain (from SMEs to larger firms) will be essential. But even with the right policies, the transition will not be painless, as diversification is a long-term endeavour and productive capacity cannot be quickly reallocated without some labour and capital losses. This is especially true in an industry as specialized and regionally concentrated as Ontario's manufacturing sector. In the meantime, patience and preparation for the rebound will be key.