TD Wealth

Red Light, Green Light

Monthly Perspectives
August 2025

15 minutes

Red Light, Green Light

Automakers, once champions of U.S.-led globalization, are now caught in the crosshairs as the new administration forces them to quickly reimagine the way they do business.

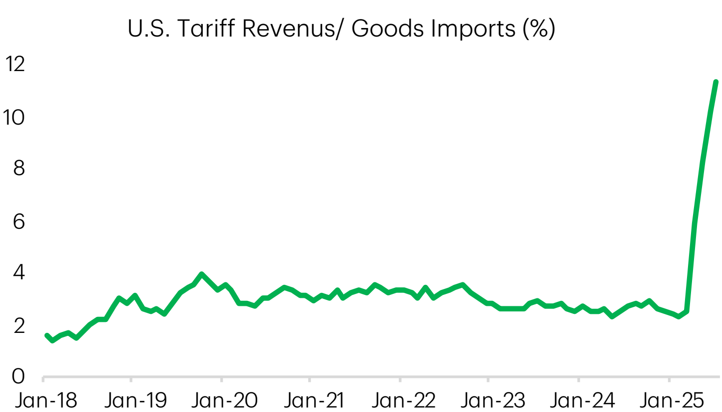
By Brad Simpson, Chief Wealth Strategist; Chadi Richa, Senior Equities Analyst | TD Wealth

Remember the debate? Was the new president serious, or was it all a bluff? Would he really undermine the bulk of the American economy — one increasingly oriented to services and innovation — in order to turn back the clock to a bellicose late-19th century, a world that saw high protective tariffs that shielded labourers from foreign competition. Would he overturn the global economic order that in the post-war era has brought the United States so much wealth and power?

Trade negotiations are ongoing, but the verdict is already in. Yes, he's serious. Yes, he would. While it's true that many of the deals announced recently feature lower tariffs than those announced on "Liberation Day," the point remains: a minimum 15% tariff rate is here to stay.

For perspective, that's four to five times higher than at the beginning of the year (Figure 1). In the most recent deal with the European Union, for instance, negotiations resulted in a 15% tariff on goods imported from the region — seven times higher than the 2% rate at the beginning of year, albeit lower than the 30% threatened.

Figure 1: The New American Economic Regime



Source: Macrobond, TD Securities
*Assumes unchanged imports for latest month

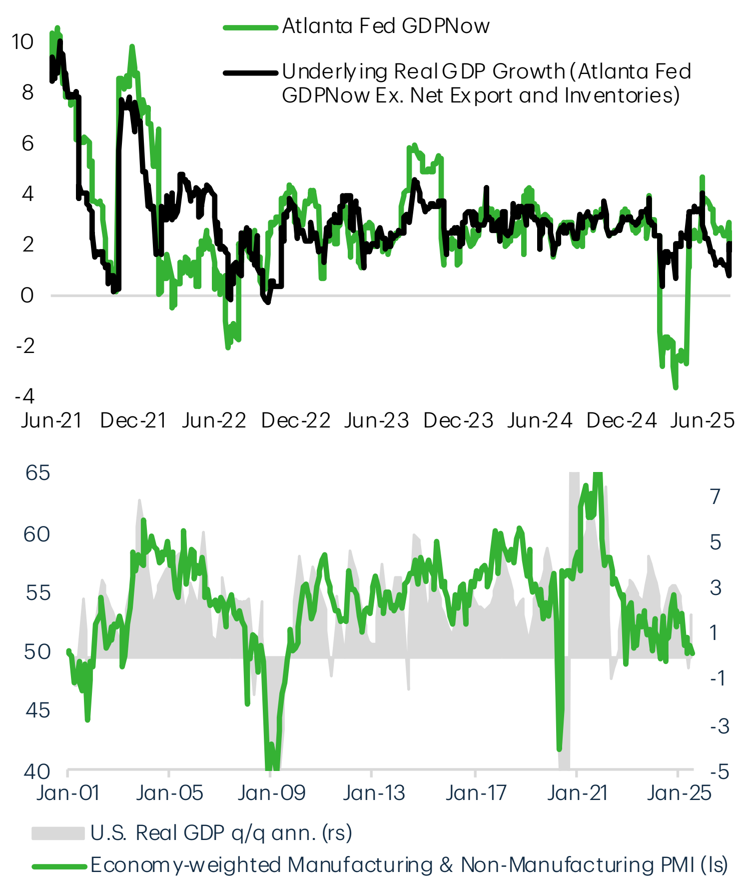
The primary impact will manifest in price increases. Already, about three-quarters of U.S. businesses that saw tariff-induced cost increases passed along at least some of these higher costs to their customers by increasing output prices. Almost one-third of manufacturers and about 45% of service firms reported passing along all tariff-related cost increases.

Supporters of the new regime may suggest that dire predictions around inflation are overblown. After all, the American economy seems to be chugging along just fine, with 2% growth reported most recently by the Atlanta Fed — but as with most things economic, the delay between policy and data can take months to years.

Already, we can see the slowdown in weakened labour growth and business confidence. In July, non-farm payrolls reported a meagre 74,000 new jobs — significantly fewer than the 110,000 that economists had expected, not to mention the 300,000 monthly gains being generated in the euphoria following the pandemic. Moreover, the job numbers for the previous two months were downwardly revised by 258,000 (much to the chagrin of the new administration, which fired the chief statistician as a result).

As for business confidence, surveys from the ISM purchasing managers' index (PMIs) — which ask managers to look forward six months — indicate stalling economic growth (Figure 2). This weakness seems to have been masked in part by the tariff front-loading that led to a surge of business prior to the new regime, but inflation will most likely rise in the coming quarters.

Figure 2: Flash GDP estimate still healthy, but PMIs bode ill

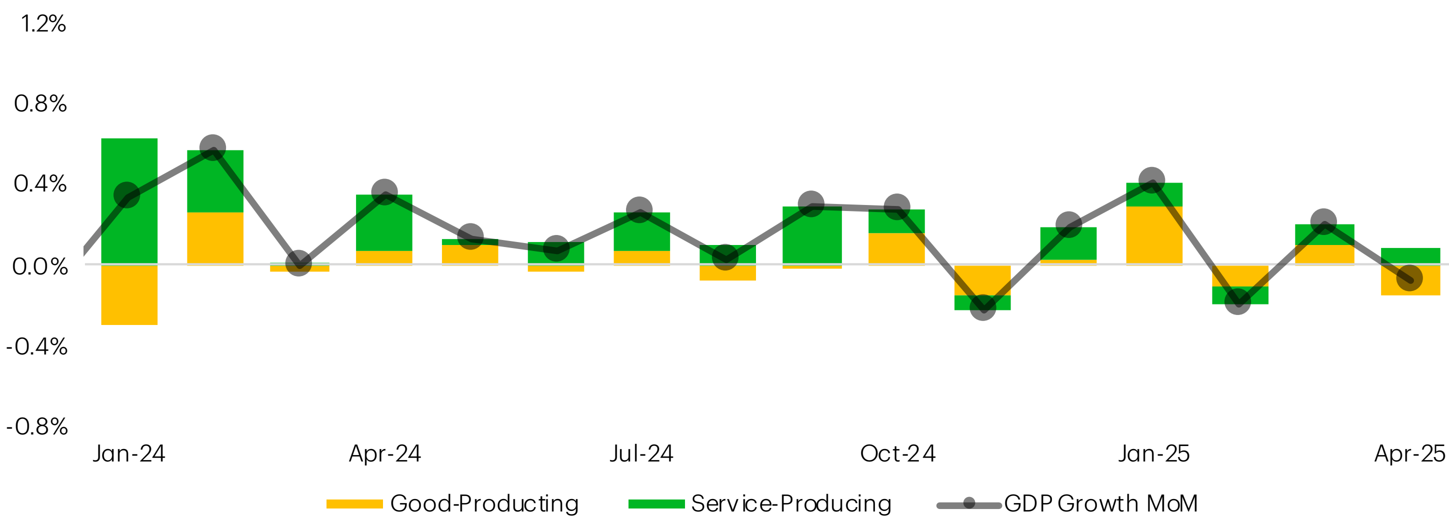


Source: Macrobond, WIO, as of August 7, 2025

In Canada, meanwhile — where nearly 70% of exports go to the U.S. — the ongoing tariff negotiations are fraught with uncertainty. In fact, it feels a bit like the game Red Light, Green Light, where one child yells out a colour and the other has to quickly react. Canadians want to know what the tariffs and their impact will be. Economics can provide some answers: Based on monthly GDP estimates, the Canadian economy shrank about 0.1% in April and another 0.1% in May, with manufacturing the most severely impacted sector (Figure 3).

Tariff uncertainty has also weighed on Canadian consumers, with most indicators now pointing to a recession in the quarters ahead. The latest TD debit and credit card spending data suggest that Canadian consumers hit pause in Q2, reacting to escalating trade tensions. On a year-over-year basis, card spending growth slowed sharply to 1.5% in Q2 from 5.4% in Q1. This reflects a growing softness in the underlying economic conditions — especially the weakening labour market.

Figure 3: Negative data already emerging in Canada



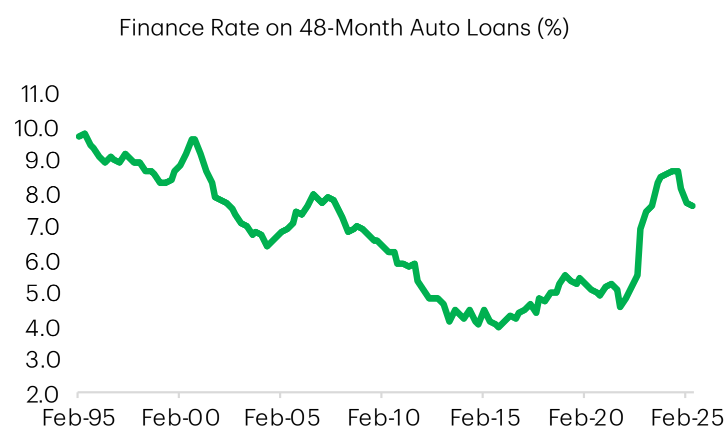
Source: Macrobond, Wealth Investment Office as of June 30, 2025

Bewildering — that's the word, I think. Amid the litany of bleak data points, there's a tendency to get lost in the woods, disoriented by the scope of it all. That's why, this month, we decided to home in on a sector that's near and dear to most Canada, and that's likely to see the greatest impact from tariffs in North America: the automotive sector. In the pages that follow, our senior equities analyst Chadi Richa takes a deep dive into what the new tariff regime means for U.S. automakers, which have spent decades building a globalized sales and manufacturing business. Richa's analysis offers a mixed picture, with serious risks and a few opportunities ahead for the carmakers.

Auto Sector in the Crosshairs

The auto industry will be one of the hardest hit by tariffs imposed by the current administration. New tariffs, from increased steel and aluminum tariffs to entirely new ones on auto imports and parts were implemented over the last three months, which led to surging demand for vehicles taxed at a lower rate. While we're yet to see clear evidence of inflation in the broader economy caused specifically by tariffs, the increase in prices in the auto market so far reflects tightening supply relative to surging demand. However, that surge in demand didn't last long. Vehicle sales slowed down in May and into June, following strong numbers in March and April, and the industry risks facing a slow down as interest rates remain high. The Federal Funds Rate remains in restrictive territory with auto rates just below 25-year highs, and unlikely to decrease until later this year (Figure 4).

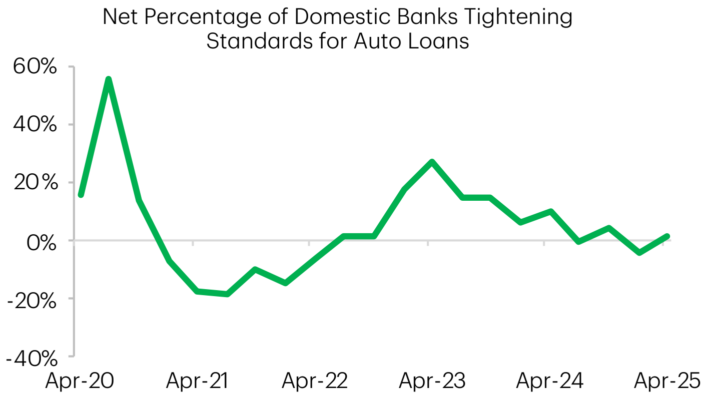
Figure 4: Auto loan rates are just below 25-year highs



Source: Federal Reserve Bank of St. Louis, Wealth Investment Office as of July 8, 2025

On the positive side, credit availability remains better than 2024 (Figure 5). Approvals are higher and there's more flexibility on loan terms, with the highest subprime participation since 2021.

Figure 5: Credit availability remains better than 2024



Source: Federal Reserve Bank of St. Louis, Wealth Investment Office as of July 8, 2025

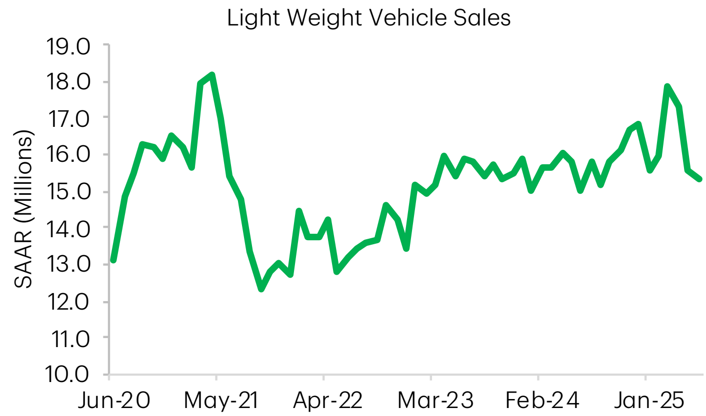
Overall, the U.S. economy remains fundamentally strong and consumer financial health is good. However, for this situation to continue the labour market must not deteriorate significantly. According to Cox Automotive, the new tariffs are expected to add collectively about US$5,700 to the cost of the average imported vehicle. For context, the U.S. imported approximately 8 million vehicles in 2024, or 50% of the total sold. Trends in new vehicle affordability have shown improvements in 2024 due to lower vehicle prices, wage growth and interest rate cuts. However, the tariffs will likely disrupt this trend, and without meaningful gains in wages and further easing of rates, it's very likely that affordability will restrict demand.

The segments that depend most on imports sit at the two ends of the price spectrum: the most affordable vehicles and luxury vehicles. While high income households can absorb the price increase, most of the vehicles priced under US$30,000 would face added costs that would make them unaffordable, which acts as another headwind for low-income consumers. Overall, U.S. consumers are more price sensitive than they were in 2020 and 2021 due to inflationary pressures and higher interest rates.

New Vehicle Market

Sales of new vehicles have been running well ahead of 2024's pace but this is expected to change. The market has averaged a Seasonally Adjusted Annual Rate (SAAR) of 15.7 million units for the first two months of 2025. Following the tariffs announced in March, vehicle buyers rushed to the market to beat potential future price increases, lifting sales in March and April to an average of 17.5 million, the highest level since the spring of 2021 (Figure 6). Sales in May and June fell to an average of 15.5 million, the slowest in 10 months. While sales increased 4.7% year-over-year (y/y) in the first half of 2025, the impact of tariffs on affordability (which hasn't been felt yet) is expected to slow the pace of sales in the second half of the year—along with the fact that there will be fewer summer buyers after the spring frenzy and tightened inventory will become more of a headwind in the autumn.

Figure 6: Vehicle sales jumped to the highest since 2021 before slowing



Source: Federal Reserve Bank of St. Louis, Wealth Investment Office as of July 7, 2025

For the time being, auto manufacturers are holding off on raising their prices significantly because demand remains tepid and policy hasn't been solidified yet. New vehicle inventory has trended downward during the first four months of 2025, and while it rebounded in the following months it's still down 5% y/y and 27% below 2019. In June, supply was at levels not seen since the autumn of 2023, when the market was still recovering from the pandemic supply chain shortages. Tariffs and trade regulation may slow vehicle production and resupply capabilities, keeping inventory tight and putting upward pressure on prices, which will cause sales to slow further. We're already seeing the impact of tighter supplies on pricing. Incentives relative to the average transaction price has been falling since its recent December 2024 peak, hitting 6.8% in May 2025. Given current supply pressures and incoming tariffs, even less discounting is likely over the coming months. So with higher priced inventory on the way, declining incentives, and potential supply disruptions also on the horizon, the new vehicle market is likely to see the return of inflation.

Electric Vehicle Market

Policy uncertainty is expected to create headwinds for the Electric Vehicle (EV) industry due to the looming expiration of benefits from the Inflation Reduction Act (which could dampen consumer demand and slow the pace of adoption), and the legal challenge to California's emissions waiver (which could limit the state's ability to set stricter vehicle emission standards). In the meantime, the momentum in the first half the year has been strong. Q2/25 sales increased 4.5% over Q1/25 and total EV sales for the first half of the year rose 1.5% y/y, hitting a record of 607,089.

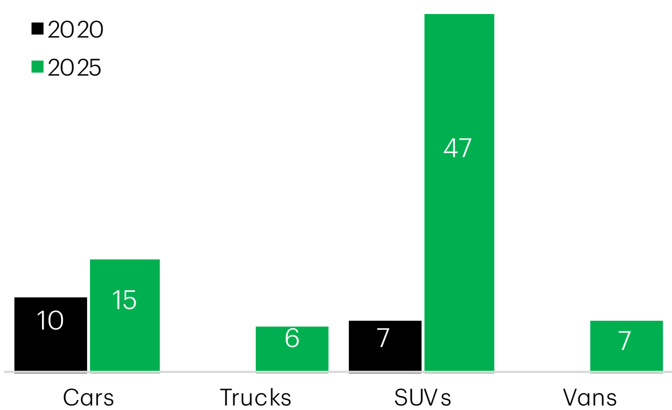
However, one positive trend has been the rapid expansion of EV model diversity; EV models increased from 17 in 2020 to 75 today, and most notable is the expansion in non-luxury, which improves affordability and increases adoption (Figure 7). EVs are also available in new segments such as SUVs, vans and trucks.

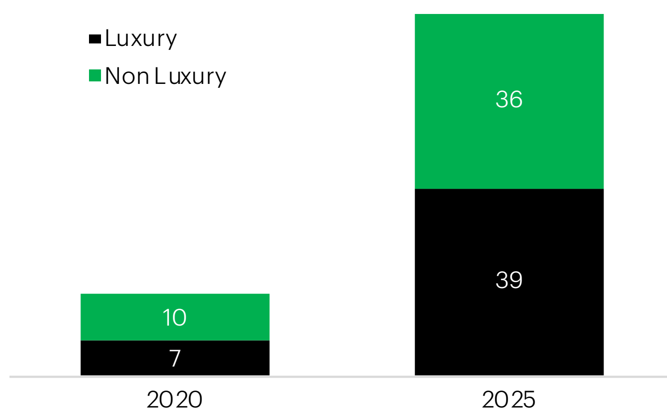
Falling prices and rising incentives are creating a buyer-friendly market for EVs, which is a profit challenge for automakers. In June, the average transaction price (ATP) for new electric vehicles dipped slightly to US$56,910, reflecting a 0.6% decrease from May and a 2.8% decline y/y, narrowing the price gap between with internal combustion engine (ICE) vehicles. EV incentives rose for the third consecutive month, reaching a record 14.8% of ATP, more than twice the incentive level offered on ICE vehicles. This underscores the continued push to make EVs more accessible amid softening demand.

Sales Performance of Manufacturers

A noticeable trend in the first half of the year was that the largest volume auto makers are seeing the largest market share gains, while smaller or more specialized companies are losing share or treading water. The outperformance of larger players is most likely driven by their large portfolio of products across many price points, which works in the current affordability-challenged market. General Motors' sales increased 12% y/y in H1/25 with a 1.5% gain in market share to 17.7%. Hyundai also had strong sales and is expected to increase market share by 70 basis points (bps) to 11%. Ford and Toyota had the strongest momentum, with sales increasing 18.3% and 22.5% respectively quarter-over-quarter (q/q). Ford's success is due to employee pricing strategies while Toyota's growth was driven by the pull-forward of demand from consumers worried about tariffs and higher prices. Stellantis is expected to see sales decline 12.7%, with Dodge and Chrysler accounting for the majority of the decline. Tesla's market share is expected to decline 70bps (Figure 8).

Figure 7: Expanding EV model diversity is improving affordability and adoption





Source: Cox Automotive, Wealth Investment Office as of June 25, 2025

Figure 8: The largest manufacturers saw the largest share gains

	Unit Sales			Market Share		
	H1/2024	H1/2025	Y/Y Growth	H1/2024	H1/2025	Change
General Motors	1,281,735	1,436,887	12.1%	16.1%	17.6%	1.5%
Toyota	1,179,653	1,244,771	5.5%	14.8%	15.2%	0.4%
Ford	1,037,281	1,108,902	6.9%	13.0%	13.6%	0.5%
Hyundai	817,805	894,361	9.4%	10.3%	10.9%	0.7%
Honda	690,281	740,823	7.3%	8.7%	9.1%	0.4%
Stellantis	677,534	591,662	-12.7%	8.5%	7.2%	-1.3%
Tesla	304,451	258,268	-15.2%	3.8%	3.2%	-0.7%
Others	1,967,830	1,905,705	-3.2%	24.7%	23.3%	-1.4%

Source: Cox Automotive, Wealth Investment Office as of June 25, 2025

Conclusion: Skillful Drivers Needed

The automotive industry accounts for over 10% of intra-regional trade in North America, equating to hundreds of billions of dollars in cross-border trade flows and millions of jobs. Tariffs are pressuring the industry, raising vehicle costs and threatening affordability, especially for low-income buyers. Demand surged briefly but slowed by June, while high interest rates, tight inventory and policy uncertainty add further strain. Large automakers are well positioned to navigate this challenging environment, primarily due to a large portfolio of products across many price points. However, the tariffs are expected to pressure margins through higher costs and dampen consumer demand.

Clearly this is a new world, and automakers face high costs as they adapt to the current reality while anticipating what a post-Trump era might look like. But if we're looking for an operative word here, it's "adapt." The auto industry is a microcosm for Canada when it comes to concerns over the impact of tariffs. For investors, this is where things get tricky. Tariffs for the auto industry are a big negative for the Canadian economy and jobs. As portfolio managers, our job is to think about the impact of tariffs on Canadian investment portfolios and what to do about it. As always, the key to surviving — and thriving — is having a well-diversified, contemporary investment portfolio built around a thoughtful wealth plan, backed by institutional-grade research, and managed by professionals employing active strategies.

Market Performance

Canadian Indices ($CA) Return	Index	(%) 1 Month	(%) 3 Months	(%) YTD	(%) 1 Year	(%) 3 Years	(%) 5 Years	(%) 10 Years	(%) 20 Years
S&P/TSX Composite (TR)	114,527	1.69	10.47	12.03	21.37	14.98	14.40	9.83	8.04
S&P/TSX Composite (PR)	27,260	1.50	9.73	10.24	17.95	11.45	11.01	6.54	4.92
S&P/TSX 60 (TR)	5,570	1.60	9.20	11.21	20.95	14.62	14.42	10.05	8.33
S&P/TSX SmallCap (TR)	1,722	1.50	15.54	14.43	18.09	11.83	13.78	8.06	4.69
S&P/TSX Preferred Share(TR)	2,334	3.19	11.40	10.72	18.25	10.03	9.94	5.48	3.45
U.S. Indices ($US) Return									
S&P 500 (TR)	14020	2.24	14.21	8.59	16.33	17.10	15.88	13.66	10.65
S&P 500 (PR)	6339	2.17	13.83	7.78	14.80	15.35	14.15	11.66	8.53
Dow Jones Industrial (PR)	44131	0.08	8.51	3.73	8.05	10.35	10.80	9.57	7.37
NASDAQ Composite (PR)	21122	3.70	21.07	9.38	20.02	19.46	14.47	15.21	12.01
Russell 2000 (TR)	12050	1.73	12.99	-0.08	-0.55	7.03	9.81	7.43	7.52
U.S. Indices ($CA) Return									
S&P 500 (TR)	19416	3.91	14.52	4.50	16.67	20.18	16.62	14.35	11.34
S&P 500 (PR)	8779	3.83	14.15	3.72	15.13	18.38	14.88	12.33	9.20
Dow Jones Industrial (PR)	61113	1.71	8.81	-0.18	8.36	13.24	11.50	10.23	8.04
NASDAQ Composite (PR)	29250	5.38	21.40	5.26	20.37	22.60	15.20	15.90	12.71
Russell 2000 (TR)	16687	3.39	13.30	-3.84	-0.27	9.84	10.51	8.08	8.19
MSCI Indices ($US) Total Return									
World	19293	1.31	12.04	11.19	16.22	16.37	14.31	11.17	8.96
EAFE (Europe, Australasia, Far East)	13194	-1.39	5.56	18.25	13.35	14.15	10.89	6.66	6.08
EM (Emerging Markets)	3364	2.02	12.94	17.90	17.87	11.02	5.85	6.19	6.57
MSCI Indices ($CA) Total Return									
World	26717	2.96	12.35	7.00	16.55	19.43	15.04	11.84	9.64
EAFE (Europe, Australasia, Far East)	18271	0.21	5.85	13.80	13.67	17.15	11.60	7.31	6.74
EM (Emerging Markets)	4659	3.68	13.25	13.46	18.21	13.94	6.52	6.83	7.23

Currency									
Canadian Dollar ($US/$CA)	1.39	1.82	0.41	-3.67	0.35	2.69	0.65	0.57	0.62
Regional Indices (Native Currency, PR)									
London FTSE 100 (UK)	9133	4.24	7.51	11.74	9.14	7.15	9.14	3.15	2.78
Hang Seng (Hong Kong)	24773	2.91	12.00	23.50	42.83	7.12	0.14	0.06	2.58
Nikkei 225 (Japan)	41070	1.44	13.94	2.95	5.03	13.89	13.60	7.15	6.39

Benchmark Bond Yields	3 Months	5 Yrs	10 Yrs	30 Yrs
Government of Canada Yields	2.69	3.02	3.46	3.76
US Treasury Yields	4.34	3.97	4.38	4.90

Bond Indices ($CA Hedged) Total Return	Index	1 Mo (%)	3 Mo (%)	YTD (%)	1 Yr (%)	3 Yrs (%)	5 Yrs (%)	10 Yrs (%)
FTSE TMX Canada 91-day Treasury Bill Index	480	0.22	0.65	1.70	3.56	4.26	2.66	1.83
FTSE TMX Canada Universe Bond Index	1177	-0.74	-0.66	0.69	2.90	2.74	-0.77	1.66
FTSE TMX Canada All Government Bond Index	1096	-0.98	-1.15	0.19	1.97	1.93	-1.50	1.21
FTSE TMX Canada All Corporate Bond Index	1472	-0.02	0.86	2.26	5.78	5.15	1.32	2.95
U.S. Corporate High Yield Bond Index	315	0.30	3.53	4.05	7.05	6.90	4.33	4.66
Global Aggregate Bond Index	263	-0.24	0.08	1.70	2.44	1.68	-0.59	1.68
JPM EMBI Global Core Bond Index	560	1.07	4.30	5.87	7.34	6.64	0.14	2.64
S&P/TSX Preferred Total Return Index	2334	3.19	11.40	10.72	18.25	10.03	9.94	5.48

Source: TD Securities Inc., Morningstar®, TR: total return, PR: price return, as of July 31, 2025.

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