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FROM TRADE WARS TO TRADE WINS

Securing Canada's economic security in the Trump era

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Canada urgently needs a new trade policy and a strategy to work with President Donald Trump. This is the worst possible time for Canada to be adrift, suffering as it is from a complete absence of federal leadership. As Trump ratchets up his tariff threats (first 10 percent, now at 25 percent), his rhetoric about the 51st state, executive orders for an America First Trade Policy, and his musings about annexing Canada, the federal government has checked out.

Prime Minister Justin Trudeau has already resigned and is awaiting his replacement while Canada's Parliament is closed down until March 24, so the Prime Minister is not able to confront a tariff crisis with significant new spending, supports for business, or added security measures. All he can do is tweet indignantly, threaten retaliatory tariffs, deliver speeches (lamenting Kamala Harris's loss and declaring himself a "feminist" (Tasker 2024), and convene meetings. His government will be fortunate to last more than a few weeks after the reopening of Parliament: his party trails the Conservatives by 25 percent, there are at least two confidence votes imminent, and the opposition parties are all promising to bring down the government at the earliest opportunity.

The crisis can only get worse in the months ahead with a rudderless Canada unable to respond and a trade-focused U.S. president sensing weakness.

The most likely scenario is that when a new government takes office in May, it will have to move swiftly to develop a new trade policy and a strategy to work productively with Trump. This is a tall order to be sure, but it's not all bad news. Canada currently has a tremendous opportunity to overhaul its trade policy, improve economic and border security (things it should be doing anyway), and lock in advantages on energy, innovation, and investment.

With a thoughtful strategy, Canada could benefit from a closer economic union with the world's most dynamic advanced economy – a tighter relationship that could yield improved trade and investment, stronger innovation, and greater productivity. However, if this opportunity is mishandled, the economic consequences could be devastating. Deloitte estimates the impact of the U.S. imposing 25 percent tariffs on Canada will be a loss of $275 billion in Canada's real GDP from 2025 to 2030 with 222,000 fewer jobs on average over the period (Deloitte 2024).

A 21st century Canadian trade policy must be based around three principles:

1. As a first step, secure "Fortress North America." Canada and the U.S. should move from a trade agreement to a broader and closer economic union (the free movement of goods, services, investment, and with some exceptions, people) that includes mutual regulatory recognition as well as reciprocal treatment of tax incentives and procurement. It should also include a security and military co-operation agreement, recognizing that economic security and the overall relationship is vastly more important than trade grievances. The U.S. has always prioritized security above trade and every G-7 statement reinforces that economic security is now a paramount global concern.
2. Make Canada the best place in the world in which to invest and build a business. This will require dramatically reduced taxes and the development of an industrial policy for strategic industries. Industrial policy should not be seen as a bunch of subsidies for favored industries. Instead, Canada's industrial policy should include a major overhaul of its patchwork of regulations and tax policies that are now making it hard to do business there: Canada must lower taxes and lower energy costs, make regulations business-friendly, create better incentives for R&D, make real investments in the supply chain and infrastructure, and improve competitiveness. The Trump administration will cut taxes and regulation drastically, so Canada must move aggressively to avoid being left at worsening competitive disadvantage.
3. The global trade system cannot function with countries that flout global trade rules and abuse the system – China's trade surplus reached a record high of $1 trillion in 2024, and the growing imbalances are stressing manufacturers in countries around the world. It's time to forge alliances to crack down on China or see the collapse of the global system as other countries retreat into protectionism.

This report contains specific policies and recommendations to achieve these objectives. The final issue is how to package all of this in the immediate term so that no president, not even Trump, would want to impose tariffs on a critical ally like Canada. Canada must offer these policies from a position of strength, via a credible government that will deliver on its promises (no more vague assurances that have no follow-through), and they must include real tangible benefits that are a win-win for Canada and the United States.

Here the biggest challenge is Canada's federal leadership. A lame duck prime minister and a paralyzed Parliament is a recipe for disaster. Only a new Canadian prime minister with a new mandate can completely change the narrative and perceptions of Canada in Washington, D.C. The problem of U.S. perceptions of Canada is fixable, but it requires bold new policies and a change at the top. MLI

Le Canada se trouve dans l'urgence d'élaborer une nouvelle politique commerciale et une stratégie de coopération avec le président Donald Trump. C'est le pire moment de perdre ses repères, car le pays souffre déjà d'un manque de leadership au palier fédéral. Alors que Donald Trump intensifie ses menaces tarifaires, (qu'il fixa d'abord à 10 % et fixe désormais à 25 %), ainsi que sa rhétorique du « 51e état » et sa réflexion sur une annexion du Canada, le gouvernement fédéral s'éclipse.

Le premier ministre Justin Trudeau a démissionné et attend son successeur, tandis que le Parlement demeurera inactif jusqu'au 24 mars. Il ne peut donc pas réagir à une crise tarifaire par des dépenses supplémentaires adéquates, un soutien aux entreprises ou des mesures de sécurité renforcées. Il ne peut que s'indigner par tweet, menacer des représailles tarifaires, prononcer des discours (sur la défaite de Kamala Harris en se déclarant « féministe » [Tasker, 2024]) et organiser des réunions. Après la réouverture du Parlement, son gouvernement risque de ne pas survivre longtemps, soit quelques semaines tout au plus : son parti accuse un retard de 25 % sur les conservateurs, au moins deux votes de confiance sont anticipés à brève échéance et l'ensemble des partis d'opposition s'engage à renverser le gouvernement à la première occasion.

Dans les prochains mois, la crise ne pourra que s'aggraver face à un Canada immobilisé par l'absence de direction et un président américain qui, focalisé sur les échanges, pressent cette faiblesse.

Selon le scénario le plus probable, un nouveau gouvernement au pouvoir en mai devra élaborer rapidement une politique commerciale et une stratégie de coopération fructueuse avec M. Trump. Indéniablement, le défi est grand, mais tout n'est pas perdu. Le Canada a une occasion en or de réviser sa politique commerciale, d'améliorer sa sécurité économique et frontalière (un incontournable) et de consolider son avantage en énergie, en innovation et en investissement.

Grâce à une stratégie minutieusement conçue, le Canada pourrait bénéficier d'une union économique renforcée avec l'économie avancée la plus dynamique au monde – une relation plus étroite pourrait favoriser les échanges commerciaux, les investissements, l'innovation et la productivité. Néanmoins, si la « balle n'est pas saisie au bond », les conséquences économiques pourraient être désastreuses. D'après Deloitte (2024), des droits de douane de 25 % feront chuter le produit intérieur brut réel de 275 milliards de dollars entre 2025 et 2030, entraînant la perte de 222 000 emplois.

La politique commerciale canadienne du XXI^e^ siècle doit être structurée autour de trois principes fondamentaux, énoncés comme suit :

1. *Dans un premier temps, sécuriser la « forteresse Amérique du Nord » est crucial. Le Canada et les États-Unis doivent envisager de dépasser le cadre du simple accord commercial afin de s'orienter vers une union économique étendue et intégrée (libre circulation des biens, des services, des investissements et, sous certaines conditions, des personnes). Cela impliquerait la reconnaissance mutuelle des réglementations et le traitement réciproque des incitatifs fiscaux*

et des marchés publics. En sécurité et en coopération militaire, cette union devrait inclure un accord affirmant la primauté de la sécurité économique et des relations générales sur les litiges commerciaux. Les États-Unis ont toujours priorisé la sécurité au détriment du commerce, de sorte que désormais, chaque déclaration émanant du G-7 souligne l'importance de la sécurité économique mondiale.

2. *Le Canada doit devenir le meilleur endroit au monde pour investir et créer des entreprises. Il faudra donc fortement réduire les impôts et concevoir une politique industrielle pour les secteurs stratégiques. La politique industrielle ne saurait être envisagée comme un ramassis de subventions pour les secteurs industriels favorisés. Elle doit plutôt revoir en profondeur une pléthore de réglementations et de politiques fiscales qui entravent actuellement les activités des entreprises sur le territoire national. Le Canada doit réduire les impôts et les coûts énergétiques, adopter des réglementations favorables aux entreprises, mettre en œuvre des incitatifs plus avantageux pour la R&D, investir dans la chaîne d'approvisionnement et les infrastructures et augmenter la compétitivité. L'administration Trump entend procéder à une réduction notable des impôts et des réglementations, ce qui va contraindre le Canada à adopter des mesures vigoureuses pour éviter un désavantage concurrentiel accru.*

3. *Le système d'échanges mondial ne peut fonctionner de manière optimale en présence de nations qui contreviennent aux règles du commerce international et abusent du système. En 2024, l'excédent commercial chinois a atteint le niveau sans précédent de 1 000 milliards de dollars – un déséquilibre qui met sous pression les fabricants à l'échelle mondiale. Il est temps de former des alliances pour contrer l'influence chinoise et éviter l'effondrement du système mondial alors que d'autres nations adoptent des mesures protectionnistes.*

Ce rapport présente des politiques et des recommandations précises pour atteindre ces objectifs. Mais comment rassembler ces éléments dans l'immédiat afin qu'aucun président, y compris Trump, ne souhaite imposer des droits de douane au Canada, un allié stratégique? Essentiellement, le Canada doit proposer ces politiques alors qu'il se trouve en position de force et par l'intermédiaire d'un gouvernement crédible et respectueux de ses engagements (évitant de ce fait les assurances imprécises et sans suite). Et ces politiques doivent offrir de réels avantages tangibles tant pour le Canada que pour les États-Unis.

Dans ce contexte, le principal défi réside dans le leadership au palier fédéral. Un premier ministre affaibli, associé à un Parlement paralysé, constitue une combinaison propice à une situation catastrophique. Seul un nouveau premier ministre investi d'un mandat neuf peut transformer en profondeur le discours et la perception du Canada à Washington. La problématique perception des États-Unis à l'égard du Canada peut être résolue, mais cela requiert l'adoption de nouvelles politiques vigoureuses et un changement au sommet. **MLI**

Introduction

Canadians may have been shocked at Donald Trump's threat to impose tariffs on all imported goods, including a 25 percent tariff on goods from Canada, but they shouldn't have been. Trump's election was not a fluke in American politics. We can be certain of that from the decisive results on November 5 as Trump won the electoral college, all the swing states, the popular vote, the Senate, and the House.

Trump's trade policy is certainly not a one-off either – it reflects a renewed focus on something that Trump has long been concerned about. Taking action against unfair trade is the one constant that he has been talking about for years (Appelbaum 2016). It's also the one Trump policy that President Joe Biden not only kept after he was elected but strengthened. And it's the one policy that seems to be catching on globally. Governments worldwide have developed a more skeptical view of free trade. That skepticism is partly driven by the West finally waking up to China's decades of abusive trade practices and subsidies, its IP theft, and its bullying, but it goes beyond that (Kennedy 2024; *The Economist* 2023). The E.U. has now mostly abandoned its free trade gospel (Barbero 2022) and even Japan is toughening its trade policy to attract strategic production back to its domestic market (Yamanouchi 2022). The era of globalization appears to be over.

In order to reinforce Canada's economic security, to continue to benefit from trade, and to protect its interests, the country needs a new trade policy and a strategy to work with Trump. If it stays on its current trajectory, Canada could find itself in the middle of a trade war with both of its largest trading partners simultaneously (the U.S. and China absorb 77 percent and 4 percent of Canada's exports respectively).

If it develops a thoughtful strategy, Canada could benefit from a closer economic union with the world's most dynamic advanced economy

– an integration that could lead to improved trade and investment, stronger innovation, and greater productivity. However, if this opportunity is mishandled, the economic consequences could be devastating. Deloitte estimates the impact of the U.S. imposing 25 percent tariffs on Canada to be a loss of $275 billion in Canada's real GDP from 2025 to 2030 with 222,000 fewer jobs on average over the period (Deloitte 2024). Canada's federal government is adrift; it has no leadership at the worst possible time.

Muddling through is not good enough

Trump has made at least five different tariff announcements in recent weeks, ranging from musing about across-the-board 10 percent or 20 percent tariffs unless countries do certain things, tariffs as a source of revenue for tax cuts, and most recently, talking about a 25 percent tariff to be imposed on Canada and Mexico. There will undoubtedly be many more such announcements in the weeks ahead as the Trump administration takes shape. The America First Trade Policy requires departments to initiate a comprehensive review of trade deficits, trade practices, barriers, duties, tax treatments, and IP, and provide reports to the President by April 1, 2025 (Trump 2025).

Canada is now scrambling to keep up; the Prime Minister has been threatening retaliatory tariffs after his trip to Mar-A-Lago went poorly, convening emergency meetings with premiers, dusting off the Team Canada approach, and conducting a charm offensive at all levels of government to make US policy-makers understand the importance of the Canada-US trading relationship.

However, at the federal level, beyond an aggressive communications exercise aimed at avoiding the worst impacts of any tariffs, it's not at all clear what the underlying strategy is. As a consequence, provincial premiers have initiated their own strategies with Quebec's premier reaching out to Trump directly, Alberta's premier talking up the advantage of North American energy independence and visiting Mar-A-Lago herself, and Ontario's premier threatening to cut off electricity exports. It all seems very piece-meal and improvised.

To be fair, Canada has announced tariffs on electric vehicles (EVs), steel, and aluminum from China that are mostly identical to U.S. tariffs in the hopes of "aligning with U.S. policy." Its federal government has just completed consultations on protecting Canada's economic security and instigated new consultations on whether to impose tariffs on a broader array of components from China, including everything from solar cells to semiconductors (Finance Canada 2024). As then-Deputy Prime Minister Chrystia Freeland said, "We are living in a world right now where China is taking advantage of the global economic system," adding, "We know we need to defend our national interest, and we will" (Zimonjic 2024). Industrial policy has replaced free trade as the dominant mindset.

> *Canada urgently needs to think through what it is trying to achieve with trade policy and to set some realistic goals.*

A new Canadian government will have to move swiftly. Canada urgently needs to think through what it is trying to achieve with trade policy and to set some realistic goals. Is it simply doing the minimum to assuage the Trump administration? Is it going to align with the U.S. and build a "Fortress North America"? Or is it trying to diversify trade? Does it need to prioritize economic security and reduce its supply chain dependence on China? Will it try to establish these industries in Canada or is it "friend-shoring"? Does Canada remain committed to rules-based multilateral trade and reforming the World Trade Organization (WTO) through its leadership in the Ottawa group? Or has it given up on the WTO after years of paralysis?

A well-crafted trade policy is crucial for prioritizing Canada's economic security and its interests in order to maximize its leverage and mitigate the potential damage in the event that it finds itself in a trade war with the United States. In the short-term, Canada must ensure that it protects domestic industries and jobs while minimizing disruptions to supply chains and consumer prices. If it gets the policy wrong, it could be stuck with the consequences for years to come – and the immediate impacts of the Trump tariffs could be damaging for the Canadian economy.

Trump's tariff threats need to be taken seriously

Even before taking office, Trump's allies such as former U.S. Trade Representative Bob Lighthizer have been trying to convince policy-makers on Capitol Hill that tariffs can have a positive economic impact and that their plans for dramatically higher tariffs "will energize the economy instead of tanking it" (Bade 2024).

Advisers close to Trump have been in discussions with House Ways and Means Chair Jason Smith on a broad tax package that will be partially paid for by tariffs. That package would include $4.6 trillion of expiring Trump tax cuts and several other tax proposals, including removing the "tax on tips" and eliminating taxes on Social Security, etc. Trump repeatedly pledged on the campaign trail to use tariffs to help pay for those tax cuts (Bade and Guggenheim 2024).

Even if legislation is complicated, controversial, or takes time, presidents have the power to raise tariffs through a variety of laws. The most often cited three are as follows:

1. The *Trade Expansion Act* of 1962 (Section 232) permits the president to impose tariffs based on a recommendation by the U.S. Secretary of Commerce if "an article is being imported into the United States in such quantities or under such circumstances as to threaten or impair the national security."
2. The *Trade Act* of 1974 (Section 301) allows the president to take appropriate action, including tariff-based, to address any unfair act, policy, or practice of a foreign government burdening U.S. commerce.
3. An "unusual and extraordinary threat" to national security, foreign policy, or the U.S. economy would be sufficient under the *International Emergency Economic Powers Act* of 1977 for the president to impose tariffs (Congressional Research Service 2016).

Why Trump's tariffs will fizzle (eventually)

The first and most important reason that tariffs will (eventually) fizzle out is that no matter what Trump says, tariffs are paid by the importer – the U.S. business or consumer. Research from UCLA examined the tariffs on washing machines, solar panels, aluminum, steel, and goods from the European Union and China imposed in 2018 and 2019. The researchers found that "U.S. firms and final consumers bore the entire burden of tariffs and estimated a net loss to the U.S. economy of $16 billion annually, including more than $114 billion in losses to firms and consumers" (Fajgelbaum and Khandelwal 2016), which were offset by small gains to protected producers and revenue gains to the government. In some cases, notably goods with higher profit margins, retailers can lower prices to offset some of the tariff impact, but still, "U.S. tariffs continue to be almost entirely borne by U.S. firms and consumers" (Amiti, Redding, and Weinstein 2020). There is a very good reason that Democrats have called Trump's tariff policies "the Trump Sales Tax."

Second, if Trump were to follow through with the tariffs he proposes, it would lead to massive inflationary pressures: an across-the-board 20 percent (or 60 percent) price hike on $3.8 trillion of imported goods and services – 17 percent of the economy. The Peterson Institute for International Economics modeled the impact of Trump's more modest proposal of 10 percent across-the-board import tariffs and 60 percent tariffs on imports from China. It found that under the Trump plan, inflation would rise from a forecast 1.9 percent in 2025 to between 6.0 and 9.3 percent (McKibbin, Hogan, and Noland 2024).

Third, Trump's assumption that tariffs encourage industries to repatriate is also very questionable. Consider a U.S. company that can manufacture and sell a product more competitively than foreign competitors only because the foreign product faces a tariff. Should the company build a new manufacturing facility to expand production to benefit from tariff protection? Doing so depends on a number of questions, specifically:

- How long does it take to build a new factory?
- How long will the tariffs last? Could they be modified or reduced?
- Will Trump change his mind about these particular tariffs?
- Will there be exceptions for certain importers?

- How much more expensive is U.S. manufacturing compared to that in Asia? Would a U.S. shoe industry be competitive, for example?
- Is it possible that another country, say Vietnam or Poland, could produce these goods more cheaply in a few years?

The point is that if the business case for a product's profitability depends entirely on a tariff, then the company owner is facing enormous political risk if he or she relies on that tariff. How many manufacturers will spend a hundred million dollars and three years to build a new factory in the hope that the tariff will last for a decade so that they can get a return on investment? Doing so seems like a dubious proposition.

The fourth problem with tariffs is that they hurt U.S. competitiveness by increasing the cost of inputs. Trump's 2018 tariffs on steel and aluminum actually led to a reduction in U.S. manufacturing employment because of higher costs for companies using steel and aluminum in their products, according to a study by the National Bureau of Economic Research (Cavallo, Gopinath, Neiman, and Tang 2019). Top U.S. businesses like Apple need global supply chains pulling in the best components from around the world. By cutting off access to foreign imports, tariffs could potentially raise the cost and lower the quality of U.S. goods. Worse, competition among firms to source tariff-free products could lead to shortages and recreate some of the supply chain problems of 2020.

Finally, tariffs are a poor source of revenue because of the distortionary substitution and growth-dampening effects of reduced trade and because of retaliation by the trading partner. Modeling at Indiana University showed that trade taxes can beneficially replace only 16 percent of the domestic tax revenue for the average country. "After retaliation, trade tax revenues decline by 50%. The domestic tax base also shrinks by 3%, prompting governments to raise domestic taxes to maintain real government expenditure. Real aggregate income also drops in all countries by around 7% on average. Altogether, after retaliation, every \$1 million of domestic tax revenue that is replaced with trade tax revenue imposes an excess burden of \$2.5 million on the economy" (Lashkaripour 2020).

None of this is new. In fact, the evidence of the harmful economic effects of protectionism and tariffs has been pretty solid over the past 250 years (Yueh 2018). So why are tariffs back in fashion?

U.S. trade policy transformed

It used to be bi-partisan economic orthodoxy that the U.S. was the biggest beneficiary of free markets and free trade. Republicans and Democrats alike basically agreed that open markets encouraged trade and investment which generated enormous gains in wealth. The United States, with a huge consumer market and so many competitive multinational companies, was obviously a big winner from trade liberalization and therefore the job of American political leaders was to negotiate as many free trade agreements as possible.

But now that many feel that "Reaganomics is on its last legs," the only thing Republicans and Democrats seem to agree on is that "trade has gone too far" (Karma 2024). Vice President Kamala Harris voted against the U.S.-Mexico-Canada Trade Agreement (USMCA) when she was in the senate and during the 2024 campaign, she promised to continue Biden's protectionist approach to trade policy, while Trump is promising to impose tariffs of 10 or 20 percent across the board along with 60 percent on goods from China. Economists have warned that these will have harmful effects on inflation, but no one in Trump's administration seems to care (Crowley 2024).

"Economists have warned that [tariffs] will have harmful effects on inflation, but no one in Trump's administration seems to care.

According to a Pew Research survey conducted in April 2024, a 59 percent majority of Americans say the United States "has lost more than it has gained from trade" (Gracia 2024). However, far fewer Americans fear competition with Canada or Europe or other advanced economies. A separate Pew Survey showed that nearly half of Americans (47 percent) said that "China benefits more from the U.S.-China trade relationship than America does. Only 14% said the same of U.S. trade relations with Canada" (Gracia 2024).

The trouble with China

The most compelling examples, objections, or problems with trade, and the most negative impacts on workers, all emanate from abuses by China. Some economists minimize the China problem by comparing trade with China to trade with other countries in the past, that complaints about China today are similar to what people said about Japan in the 1980s or Mexico in the 1990s. This is not accurate. China has distinguished itself by the scope, scale, and intensity of the abusive practices through which it has become a global trade superpower. Its overall trade surplus is a staggering all-time high of U.S.$1 trillion and it sells more than it buys from 165 countries around the world (Bloomberg News 2025). Specifically, China is:

Artificially devaluing the renminbi to make exports more competitive (U.S. Department of the Treasury 2019).

Last year, China exported $563 billion to the United States and imported only $196 billion. Normally, such a huge current account surplus (and U.S. current account deficit) would cause the currency to appreciate against the dollar. For example, in the mid-1980s Japan's trade surplus in cars and electronics caused a significant appreciation in the yen which made their exports much more expensive. This took some of the pressure off U.S. manufacturers and resulted in recession in Japan. The Japanese word for this is *endaka fukyo*, which means a recession caused by a strong yen (Obstfeld, 2009).

But there has been no appreciation in China's currency because the exchange rate is fixed within a narrow band against a basket of currencies by China's central bank. Maintaining the same exchange rate (roughly 6–7 RMB/USD over the past 15 years) requires huge distortions in the capital account (Setser 2024).

Indeed, China has a massive current account surplus estimated at a staggering $900 billion annually against the rest of the world. It is supported by purchases of foreign securities that are even larger than the official figures as the People's Bank of China and other state-owned banks buy up massive amounts of U.S. treasuries and other highly rated securities (Setser 2023). According to the World Bank (2024), China has now accumulated an alarming $3.4 trillion of foreign exchange reserves and an additional $2 trillion of bonds held by state-owned banks, yielding investment income of $100 to $140 billion annually. This means that China can continue to pile up massive trade surpluses without any appreciation in the currency because they are offset by gigantic current account surplus of almost the same amount, as high as $800 billion (Setser 2023).

Massively subsidizing export industries.

China's industrial subsidies, from standard fiscal subsidies to tax breaks to discrete uses of financial credit are enormous, totaling at least $248 billion annually (approximately 2 percent of GDP and equivalent to more than $407 billion at purchasing power parity exchange rates.) This is higher than China's defense spending (Dipippo, Mazzocco, and Kennedy 2022).

As a result, China has achieved strategic dominance in a number of key industries. China produces over 80 percent of the components for the world's solar cells after investing an astounding US$130 billion into the solar industry in 2023. China controls more than 80 percent of battery manufacturing capacity, followed by the U.S. and the E.U. with around 5 percent each. It is not possible in the short or medium term to find alternative suppliers for thousands of electronic components in everything from EVs to cell phones (Wood Mackenzie 2023).

Engaging in wide-scale, systemic, state-sponsored theft of intellectual property.

Canada's Communications Security Establishment warns that "China's aggressive cyber program presents the most sophisticated and active state cyber threat to Canada today. The PRC conducts cyber operations against Canadian interests to serve high-level political and commercial objectives, including espionage, intellectual property (IP) theft, and transnational repression" (Communications Security Establishment Canada 2024). According to the FBI, China has "a bigger hacking program than that of every other major nation combined" that "together with Beijing's physical spies and stealing of trade secrets from private businesses and research institutions gave the country enormous power." The Australian Security Intelligence Organization says that "The Chinese government is engaged in the most sustained scaled and sophisticated theft of intellectual property and expertise in human history" (Siddiqui 2023).

It is China's awesome combination of the three factors – the artificially low foreign exchange rate, the enormous subsidies and unlimited lending to manufacturers, and the widespread theft of IP that has led to a historic trade surplus of $1 trillion and that has unquestionably damaged manufacturing in the U.S. and around the world. According to American Compass, “Jobs and production shifted abroad, leaving behind a weakened industrial base, eroded communities, and poor job prospects for our middle class. It has put [...] the nation on a trajectory of long-term decline, economic instability, and geopolitical risk” (DiPlacido 2024). This is backed up by economists like David H. Autor who demonstrated that a sizable increase in Chinese imports into the United States during the 2000s “eliminated more than 2 million U.S. jobs while also exacerbating addiction and other social ills in disproportionately affected communities” (Autor, Dorn, and Hanson 2016).

> *Canada is under enormous pressure to match the US tariffs.*

As a result, the U.S. has undergone a transformational shift in trade policy that began under Trump and that was further strengthened and reinforced by Biden. Perhaps the most fulsome articulation of the new perspective was U.S. Trade Representative Katherine Tai’s description of the Biden-Harris “Worker-Centered Trade Policy” (Tai 2021). It seeks to set a high standard alternative to state-directed economies that do not promote the rights of workers; it aims to combat forced labor while “more effectively responding to the threats of autocratic, non-market countries whose policies undercut our workers.”

This is not just rhetoric. On May 14, 2024, the Biden administration announced significant tariffs on a wide range of Chinese-manufactured goods. These include a 100 percent tariff on Electric Vehicles (EVs), as well as increased tariffs on batteries, semiconductors, aluminum, steel, and other key products. The E.U. has instigated similar tariffs on China’s EVs.

Canada is under enormous pressure to match the U.S. tariffs to avoid being seen as a back-door way for Chinese imports to enter North America, and it needs to protect the auto industry in light of its substantial $52.5 billion commitment to support EV investment (Giswold 2024). Elon Musk’s warning that Chinese EV firms could “demolish” competitors in the absence of trade barriers further underscores the urgency for Canada to act.

TABLE 1: Biden administration tariffs

Sector/products	New tariff rate	Effective date	Old tariff rate
Steel and aluminum	25%	2024	0–7.5%
Semiconductors	50%	2025	25.0%
Electric vehicles (EVs)	100%	2024	25.0%
Lithium-ion EV batteries	25%	2024	7.5%
Lithium-ion non-EV batteries	25%	2026	7.5%
Battery parts	25%	2024	7.5%
Natural graphite and permanent magnets	25%	2026	0.0%
Certain other critical minerals	25%	2024	0.0%
Solar cells	50%	2024	25.0%
Ship-to-shore cranes	25%	2024	0.0%
Syringes and needles	50%	2024	0.0%
Certain personal protective equipment (PPE)	25%	2024	0–7.5%
Rubber medical and surgical gloves	25%	2026	7.5%

Source: White House 2024

Rough waters ahead: reviewing USMCA

Not only do hard decisions have to be made about trade with China, but at the same time Canada is about to embark on negotiations to review the U.S.-Mexico-Canada Trade Agreement (USMCA) with a trading partner that is hyper-sensitive about trade and willing to tear up agreements.

Even before taking office, Trump had already promised to renegotiate USMCA: "Upon taking office, I will formally notify Mexico and Canada of my intention to invoke the six-year renegotiation provision of the USMCA that I put in […] I want to make it a much better deal. I want to take advantage, now, of the car industry," he said (Lobosco 2024). More recently, his executive order, the "America First Trade Policy," which took effect on January 20, 2025, orders the U.S. Trade Representative to immediately begin the public consultation process required in the review of USMCA and to provide a report back to the President by April 1, 2025 (Trump 2025).

The review clause in USMCA is unique and unprecedented. Six years after it was implemented (in 2020), USMCA requires a formal review at which time all three governments must agree to renew USMCA for another 16 years. If not all states agree, then there are to be annual reviews for the next 10 years until USMCA is cancelled (in 2036). If there is an agreement, then the next review is in six years.

The risks of this approach is that it will undermine investment in North America. The purpose of a trade agreement is to bring certainty and stability and to protect trading partners from political whims by having a permanent arrangement. Major investments in plants and manufacturing are 40-year decisions that assume permanent market access. Uncertainty chills investment and reduces integration because of the risk of disputes and countries withdrawing.

The six-year review reinjects politics into North America's most important trade agreement by ensuring that a massive dose of political misery will come up every presidential election cycle.

What does the USMCA review process look like?

Leaving aside the exaggerated political rhetoric in an election year, there are many questions about the review process and each party can decide what it wants to do in the lead-up to the USMCA review.

But the difference in approach between Canada and the United States could not be starker. Canadian officials are carefully managing expectations (downward) and seem to want to avoid rocking the boat. Last year, when the author reached out to officials at Global Affairs Canada to ask how business could support or provide input into the USMCA review, he was told: "This is not a reopening. It's an opportunity to discuss how to make sure the Agreement remains relevant in the future. At this time, we are focused on ensuring the continued implementation of the Agreement." Ho hum, nothing to see here.

Contrast that with a recent speech by current U.S. Trade Representative Tai who warns of tough negotiations coming: "We're working hard and getting ready. We need to have discomfort and uncertainty in order to motivate the parties to address issues and improve the trade agreement. The whole point is to maintain a certain level of discomfort – which may involve a certain level of uncertainty. To keep the parties motivated to do the really hard thing, which is to continue to re-evaluate our trade policies and trade programs ... That discomfort is actually a feature – not a bug" (Tai 2021).

> *The biggest risk for Canada is the central incoherence in US trade policy.*

Tai seems to be saying that only with an uncomfortable confrontation and uncertainty about the future of USMCA will tough issues be resolved. While her approach is undoubtedly preferable to Trump's threats to "destroy the auto industry," "punish the people of Canada," or his striving to "humiliate" the prime minister, it seems that Tai's best-case scenario for the USMCA review is a series of aggressive U.S. demands for new concessions and continued bickering over North American free trade, all reinforced by the underlying threat to cancel the whole agreement (Kay 2018).

What does this mean for Canada?

The biggest risk for Canada is the central incoherence in U.S. trade policy: American policy-makers point out that China's massive subsidies, IP theft, and dumping, are damaging the U.S. manufacturing sector and undermining national security. U.S. allies almost unanimously say, "we agree, it's time to crack down on China." But then the U.S. turns around and hammers its allies with ill-considered policies that barely bother China at all.

Four years after threatening to tear up NAFTA and exiting the Trans-Pacific Partnership (the forerunner to the Comprehensive Progressive Trans Pacific Partnership or CPTPP), the U.S. now has a new industrial policy with lavish subsidies for favored industries, major tax incentives for products built domestically, and the *Build America, Buy America Act* that requires that all of the iron, steel, manufactured products, and construction materials used in federally funded infrastructure projects are produced in the United States (Siripurapu and Berman 2021),

It's time for Canada to take a new approach, one designed for the challenges of the 21st century: a multi-faceted trade, economic, and security alliance with the U.S., a partnership with which to crack down on cheaters who abuse the system of international trade, and a link between Canada's trade priorities and industrial policy.

A new trade policy for Canada?

Canada's trade policy for the 21st century must be based around three principles:

As a first step, secure "Fortress North America."

Canada and the U.S. should move from a trade agreement to a broader and closer economic union (the free movement of goods, services, investment, and with some exceptions, people) that includes mutual regulatory recognition as well as reciprocal treatment of tax incentives and procurement. It should also include a security and military co-operation agreement, recognizing that economic security and the overall relationship is vastly more important than trade grievances. The U.S. has always prioritized security above trade and every statement it makes at G-7 meetings reinforce that economic security is now paramount.

Make Canada the best place in the world in which to invest and build a business.

This will require dramatically reduced taxes and the development of an industrial policy for strategic industries. Industrial policy should not be seen as a collection of subsidies for favored industries. Instead, Canada's industrial policy should include a major overhaul of its patchwork of regulations and tax policies that are now making it hard to do business in the country: Canada must lower its taxes and lower its energy costs, make regulations business-friendly, create better incentives for R&D, make real investments in the supply chain and infrastructure, and improve competitiveness. The Trump administration will cut taxes and regulation drastically, so Canada must move aggressively to avoid being left at an even further competitive disadvantage.

The global trade system cannot function with cheaters who are abusing the system.

It's time to forge alliances to crack down on China or see the collapse of the global system.

Implementation and action plan

Approach the U.S. with the "big picture," a plan for a North American economic and security powerhouse, not a defensive list of grievances

Canada has much to offer the U.S. – from energy independence to economic security, from the military partnership and NORAD to vital components of the electrical supply chain, IP, technology partnerships, rare earths, and uranium to power U.S. nuclear plants.

It's time to think strategically about North America as a trade, manufacturing, IP, and energy superpower. Canada and the United States share one of the world's most comprehensive trading relationships, rooted in close geographic proximity, cultural ties, and interdependent economies. Establishing an economic union between the two countries could amplify these benefits, creating a more seamless flow of goods, services, and investment across borders. Such a union would reduce trade barriers, harmonize regulations, and increase competitiveness in global markets, particularly against economic giants like China and the European Union. Additionally, a unified economic framework could foster innovation through shared resources and enhance energy security by optimizing the use of North America's abundant natural resources. By leveraging each country's complementary strengths, an economic union could drive sustainable growth and improve job opportunities, and both countries could work together on clean energy incentives to foster North American supply chains that would help protect industries against dumping from China.

As Canada prepares to enter the USMCA negotiations, it is critical that it seize this opportunity to reinforce the economic security Canada can help provide; Canada is a stalwart ally with a plan to increase defense spending to two percent of GDP, and it is a staunch defender of North American economic sovereignty and friend-shoring.

If Canada has a clear plan to make North America a trade and manufacturing powerhouse, with generous incentives for manufacturing and innovation, and if it is willing to invest Canadian money to build stronger North American supply-chain infrastructure to compete with China and enable near-shoring, Americans will be interested to hear about it.

Such a plan would enable Canada to advocate for friend-shoring, thereby ensuring reciprocal benefits (i.e., inclusion in U.S. tax incentives for domestic content), which would make sure that Canadian companies could benefit from the same advantages as their U.S. counterparts. Strengthening both countries' mutual trade relationships will enhance economic security and support the development of North American supply chains.

Strengthen the border with real measures that show Canada is serious

Trump's top concerns are poorly secured borders and combatting the flow of fentanyl into the U.S. He evidently told Quebec Premier Francois Legault that tariffs could be avoided if Canada would only strengthen the northern border (Prince 2024). More importantly, a stronger border would protect Canadians.

Canada could strengthen its border to help deter the influx of illegal drugs, illegal immigration, and crime by investing in several key areas. First, it could enhance the technological capabilities of the border system with AI-powered screening tools, advanced imaging technology, and chemical detection devices that would improve the identification of illicit substances and contraband. Second, it could increase the number of trained border patrol officers and canine units, which would bolster physical inspection capacity. Third, it could expand intelligence sharing and collaboration with U.S. law enforcement agencies, which would help disrupt cross-border criminal networks.

Finally, it is time to reverse Canada's experiment with decriminalizing hard drugs. That initiative has proven to be a tragic mistake; Canada has suffered a devastating toll of 47,000 overdose deaths since 2016, which serves as a stark reminder of the policy's failure. The policy not only failed to curb addiction rates – it has also exacerbated the crisis. To protect Canadians, particularly vulnerable youth, it is imperative to reverse this misguided approach. Reinvesting in treatment programs, expanding access to harm reduction services, and implementing stricter law enforcement measures against drug traffickers are essential steps to address this public health emergency and safeguard the lives of Canadians.

Become the necessary trading partner

Canadians haven't forgotten that at the height of the COVID-19 pandemic, the Trump administration blocked exports of N95 masks to Canada. The premier of Ontario gave a shell-shocked press conference at which he vowed never to depend on another country ever again (*CTV News* 2020). What ended the export restrictions was not Canada's relationships, its lobbying, or its friends in U.S. government. It was that Canada supplied the specialized medical-grade pulp fiber that was essential to making N95 masks and other protective medical supplies (Keller and Hunter 2020). Simply, it was impossible for some U.S. manufacturers to produce the masks without Canada's essential inputs into the supply chain (Canadian Press 2020).

In crafting its updated industrial policy, the government of Canada needs to focus on things that other countries absolutely need. Canada provides the uranium that powers U.S. nuclear reactors, the oil that makes the U.S. energy independent, leading-edge AI models, and other critical parts of the supply chain. But it needs to do much more: it must accelerate the production and mining of rare earth minerals and expand Canadian manufacturing and energy production to make Canada an essential partner so that any real breakdown in the trading relationship becomes almost unthinkable to the United States.

Make Canada competitive again – reduce taxes and regulation while investing in industrial policies that support Canada's key export sectors

When Trump won the most recent presidential election, the Dow Jones Index shot up 1500 points thanks to investors who expect he will implement more market-friendly policies, such as "lower corporate tax rates, deregulation and industrial policies that favor domestic growth" (CBS News 2024). More concretely, Trump's executive orders slash regulation dramatically, ordering agencies to expedite all approvals, sweep away regulatory requirements, invoking emergency powers if necessary to move ahead with energy and natural resource projects (Trump 2025).

Canada's competitiveness woes are about to become much more serious if Trump's agenda to turbo charge U.S. business is combined with aggressive U.S. tariff policies. Canada urgently needs to implement measures to improve its competitiveness; it also needs to build a comprehensive industrial policy to effectively compete and trade with the United States, regardless of potential tariff changes.

While the current federal government's industrial policy has focused on narrow subsidies – to the tune of a staggering $52.5 billion to support electric vehicle factories – a robust industrial policy should extend beyond this approach.

A successful industrial policy involves cultivating the entire ecosystem necessary for industry growth which Canada can do by lowering taxes and reducing regulation, ensuring sustainable access to raw materials and resilient supply chains, securing low-cost energy and essential inputs, and developing a skilled workforce ready to meet the demands of high-tech industries. It also includes fostering a favorable environment for research and development, supporting accessible financing and funding options for Canadian businesses, and facilitating entry to both domestic and international markets. By strategically building this interconnected foundation, Canada can create a self-sustaining industrial environment capable of thriving in a competitive global economy.

Accelerate military procurement with real transactions to demonstrate Canada's commitment to economic security

An example of where it does make sense to pursue industry favoritism is when defense and national security interests prevail. Taiwan is considering big U.S. defense purchases as an overture to Trump because the Taiwanese government wants to show the new administration it is serious about protecting itself against China. Following Taiwan's lead may be the only way that Canada can prove its commitment to security after a decade-long dithering over whether or not it should meet the two percent of GDP NATO target for defense spending—dithering that has damaged Canada's reputation (Shimooka 2023).

In July 2024, Trudeau said that Canada would meet its promised NATO defense-spending target by 2032, but he dismissed the benchmark as little more than a "crass mathematical calculation" and did not lay out a plan for how Canada would reach the target. Allies could be forgiven for being skeptical.

If Canada were to announce a major purchase of F-35 fighter jets, or if it were to join the AUKUS military alliance and purchase nuclear subs alongside the U.K. and Australia, those real investments would remove the doubts about Canada's commitment to defense. The costs for such purchases are quite significant but the benefits are enormous, and they can be spread over decades.

Most importantly, Canada urgently needs to make major investments in its military; those investments are essential for ensuring its national security. Canada's military capabilities are already deteriorating and in disarray (Shimooka 2024). In fact, in July 2024, Canada's chief of defense staff noted starkly that "Canada and the U.S. have five years to prepare for new threats from Russia and China" (Burke and Major 2024). It's time to crack down on China, but in the short-term Canada must take a measured, cautious approach until it can protect its industries and obtain necessary reassurances from the U.S.

> *It would be madness for Canada to rush into a potential trade war with China… while the U.S. is threatening to renegotiate or cancel USMCA.*

According to the Brookings Institute, the U.S., Canada, and Mexico need a more coordinated approach to their trade and investment policy with China so that their trade actions will be effective (Meltzer 2024). Until a formal agreement is in place, Canada should take a carefully calibrated approach when considering trade measures against China.

China produces over 80 percent of the components for the world's solar cells after investing a staggering US$130 billion into the solar industry in 2023 (Wood Mackenzie 2023). China controls more than 80 percent of battery manufacturing capacity, followed by the U.S. and the E.U. with around 5 percent each. It is not possible in the short or medium term to find alternative suppliers for the thousands of electronic components found in everything from EVs and batteries, to cell phones and solar panels.

Also, it would be madness for Canada to rush into a potential trade war with China and put all its economic eggs in the U.S. basket while the U.S. is threatening to renegotiate or cancel USMCA. Canada needs to get some assurances of access to U.S. markets before taking any trade action against China.

China has launched an anti-dumping probe into Canadian canola that will undoubtedly find that Canada's canola exports are guilty and deserving of significant tariffs (Reuters 2024). If Canada goes along with the U.S. in imposing tariffs on Chinese products, Canada's canola industry risks significant losses from its $3.8 billion exports to China in the face of China's retaliation. The hope is that Canadian canola can find other markets, but the situation could also get very much worse.

Canada's $8.9 billion of exports of canola and canola oils to the United States could be completely shut out next year. In September a bill was introduced in the U.S. Senate, the *Farmer First Fuel Incentives Act*, which would restrict the 45Z Clean Fuel Production Credit (which provides a tax credit for domestic production of clean transportation fuels) to only biofuels made from U.S.-produced feedstock (Marshall 2024). Once Canadian feedstocks are shut out from a subsidy of $1.00 per gallon for fuel and $1.75 per gallon for aviation fuel, Canada's exports of canola to the U.S. would be blocked from the entire U.S. biofuels industry, which would be forced to switch to U.S. canola oil.

Implement new incentives, financing, and tax credits

To encourage the return of key industries to Canada, the government should consider introducing a range of incentives, including financing options and tax credits.

Merely imposing tariffs will not lead to the spontaneous re-emergence of industries within Canada. Generous incentives similar to the U.S.'s 45X tax credits (which provide a 10 percent credit to taxpayers for costs incurred during the production of critical minerals to specified levels of purity) are essential for attracting investment and fostering the development of domestic industries. By providing robust support for industries like clean technology and advanced manufacturing, Canada can create a favorable environment for companies to invest in local production, thereby reducing reliance on foreign imports and boosting the Canadian economy. These policies could be crafted in such a way that they are compatible with WTO law – for example by not making them contingent on export performance.

Regulatory harmonization, technology, and competition

Canada can improve trade relations with the United States by prioritizing regulatory harmonization, particularly in its treatment of foreign technology companies. Ensuring a fair, business-friendly environment for these companies would strengthen Canada's economic landscape and its position at the negotiating table. Currently, policies like Canada's Digital Services Tax (DST) and the *Online Streaming Act* have sparked U.S. concerns and threats of retaliatory measures. The DST, for example, has drawn criticism due to its targeted impact on American firms, while the *Online Streaming Act* imposes nearly $200 million in annual charges on foreign streaming companies. Additionally, Canada's proposed *Artificial Intelligence and Data Act* (AIDA) introduces extensive regulations that may place a heavy burden on AI companies, many of which are based in the U.S. By re-evaluating these measures to ensure they align with international standards and do not disproportionately affect foreign businesses, Canada can foster a more favorable climate for tech investment and innovation, ultimately promoting stronger economic ties with the U.S. and heading off any potential retaliation in the next round of trade negotiations.

Continue advocating for a multilateral approach at the WTO

As a mid-sized economy heavily dependent on trade, the rules-based global trading system has a direct impact on Canadian economic growth and the well-being of Canadians. When the global rules-based trade system does not function well, that is a significant risk to Canada's trade performance.

However, the global trading system cannot function when cheaters abuse the system. Rosen, Goujon, and Wright (2024) point out that "China's growth strategy is inherently confrontational and zero sum: China is not adding to global demand but rather competing more aggressively in overseas markets. Advanced manufacturing countries whose industries are threatened by cheap Chinese goods and countries in the Global South that are fighting to move up the value chain all have clear reasons to restrict Chinese exports." Canada's success in trading with Asia and the European Union demonstrates the benefits of a multilateral trade strategy. Abandoning multilateral engagement in favor of a protectionist, North America-focused approach would limit Canada's economic opportunities and put its industries at a disadvantage.

North America needs allies who are willing to confront China. Canada is leading international efforts to reform the WTO and chairs the Ottawa Group, which is composed of 14 like-minded WTO members seeking to strengthen the organization across 3 key pillars: transparency and monitoring, negotiation and rule-making, and dispute settlement. These efforts should be refocused on promoting free trade with allies that are willing to confront countries that are abusing the system, like China.

With Mexico increasingly acting as a back door for Chinese imports, Canada must focus on its bilateral economic interests with the U.S., even if it means divorcing from Mexico

Canada's instinct in North American trade talks is often to team up with Mexico against the superpower, but that could be a big mistake, particularly now that almost all U.S. problems with trade and border control are centered on Mexico.

Customs data show there has been a massive surge in raw materials and components from China entering Mexico where they are manufactured into fully assembled items that are then transported into the U.S. Chinese companies are moving their production facilities from China to Mexico so that "They can bring in their parts and raw materials from China and then produce the product in Mexico at their Chinese facilities and then ship those goods into the U.S." (Grant 2024).

As a result, imports from Mexico to the U.S. have increased by 20 percent or more annually between 2020 and 2024. It is entirely legal for Chinese companies to add some value by operating in Mexico and taking advantage of the USMCA to have their product made in Mexico and then shipped to the United States. But the U.S. now sees Mexico as a back door to trade with China, which places it squarely in the crosshairs of U.S. trade negotiators. Siding with Mexico in the upcoming trade disputes would be detrimental to Canada's economic interests (LaRocco 2024).

Ontario's premier went even further on November 12, 2024, when he urged Canada and the U.S. to negotiate a bilateral trade deal without Mexico. Ford said, "Since signing on to the United States-Mexico-Canada Agreement, Mexico has allowed itself to become a back door for Chinese cars, auto parts and other products into Canadian and American markets, putting Canadian and American workers' livelihoods at risk while undermining our communities. [...] If Mexico won't fight transshipment by, at the very least, matching Canadian and American tariffs on Chinese imports, they shouldn't have a seat at the table or enjoy access to the largest economy in the world" (Freeman 2024).

Canada needs strong leadership – now

The final issue is how to package all of this in the immediate term so that no president, not even Trump, would want to impose tariffs on a critical ally like Canada. Here the biggest challenge is Canada's federal leadership. Even if Trudeau were a very skilled negotiator who got along well with Trump, there would still be the problem that he is a lame duck; he has resigned and now has a paralyzed, shut-down Parliament, so he is unable to deliver new spending or security measures. His party is trailing the Conservatives by almost 30 percent (Fournier 2025), and his ministers are distracted by a leadership race. The Opposition is now united and is promising to bring down the government at the earliest opportunity.

Worse, Trudeau lacks credibility on all of the issues that Canada needs to convince the Americans it cares about. Is the prime minister who legalized fentanyl in British Columbia going to suddenly crack down on drugs? Is the Liberal politician who blew up the immigration system – international students arriving with no background checks and the population rising by 1.3 million – going to suddenly seal the border and crack down on illegal migrants? Is the leader who reduced criminal sentences across the board and made bail much easier to get going to suddenly crack down on crime? No one would believe it – either in Canada or the United States. All Trudeau can offer is indignant tweets and banal reassurances. His obvious weakness has goaded Trump into making a series of suggestions that Canada become the 51st state.

Only a new Canadian prime minister can completely change the narrative and perceptions of Canada in Washington, D.C. The problem of U.S. perceptions of Canada is absolutely fixable, but it almost certainly requires a change at the top.

In the medium-term, Canada's evolving trade policy must be part of a broader economic strategy, with targeted investments to reinforce its role as a vital player in North American and global trade. It's time for Canada to accelerate its defense readiness with real investments so that its NATO partners can see concrete actions, not just hear the same complaints about the 2 percent spending target. Strengthening ties with the U.S. by promoting a vision of "Fortress North America" will emphasize Canada's economic and defense synergies, creating a robust framework that will allow Canadian industries to thrive within a collaborative but competitive environment. Confronting challenges with China by taking a balanced approach to trade with it while also securing alternative markets and supply chains will be essential to sustaining Canadian industries and protecting the country's economic interests. Meanwhile, Canada's continued commitment to multilateral engagement and reform of the WTO will highlight its proactive role in upholding a rules-based international trade system, ensuring stable growth and opportunity in an interconnected world. MLI

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Appendix A
Canada's current trade policy

At the core of Canada's current trade policy is the belief that "Expanding trade and investment is key to ensuring meaningful, inclusive and sustainable prosperity for Canadians, businesses and communities" (Global Affairs Canada 2024a). This notion that trade and foreign investment equals wealth and prosperity (hopefully for everyone) has been economic orthodoxy for decades. But more and more questions are being raised, spurred in the US by research from Autor, Dorn, and Hanson, which has demonstrated how the surge of imports from China caused the loss of 1 million US manufacturing jobs, and 2.4 million jobs overall during the 2000s. Some of these losses are surely due to automation, but the risk posed by China's industrial capacity, spurred by low wages and subsidized energy, is impossible to ignore.

The overall benefits of trade are rarely questioned in Canada despite evidence that damage to labor markets from excessive trade surpluses can be worse than most people realized (Blair and Gurevich 2021). Research shows that the direct effect of Chinese import competition in Canadian manufacturing was a total loss of 170,000 manufacturing jobs between 1991 and 2011, accelerating after 2001 when China joined the WTO (Sharpe 2017). When touting the benefits of trade, Canada must at least consider the impact on workers.

Canada's trade policy is based on three mutually reinforcing priorities:

Support for a strong, rules-based multilateral trading system

Smaller countries are best protected in a multilateral rules-based system. There is a long track record of Canada using the dispute-settlement mechanisms in the North American Free Trade Agreement (NAFTA), at the WTO, or those organized under other trade agreements, to protect its trade interests from occasional bursts of protectionism or a well-funded industry group lobbying for special protections.

However, it is also important to recognize the reality that the United States has effectively paralyzed the WTO's dispute settlement system. The US has blocked new appointments to the WTO's Appellate Body since 2016 (Díaz 2019), and it ceased being able to function in 2019. This means that WTO members have lost the right to appeal, and as a result certain members are able to block the final resolution of disputes.

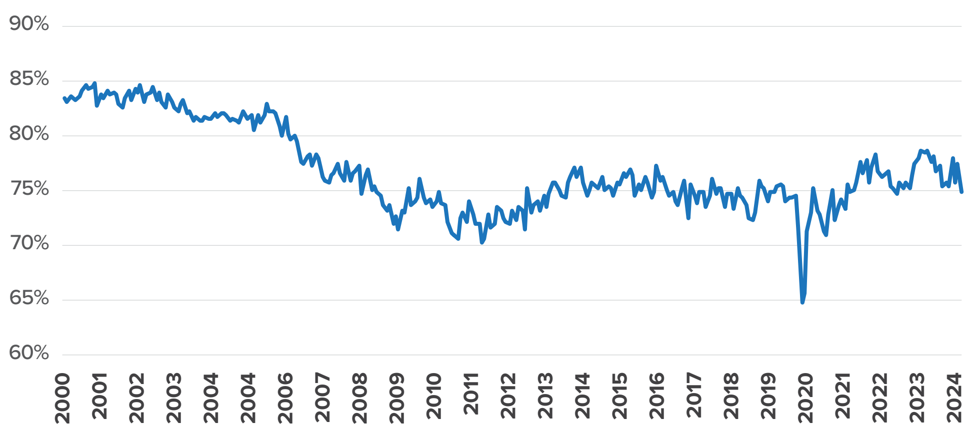
There are work-arounds: Canada, the European Union, and another 30 or so mostly developed countries have agreed to resolve disputes with an alternative ad hoc body that will review a decision that they would have otherwise appealed to the WTO. The Multi-Party Interim Appeal Arbitration Arrangement (MPIA) has already begun to issue rulings. But if Canada's largest trading partner has placed itself outside the WTO system, it may be time for Canada to reconsider its priorities.

Trade diversification

Trade diversification has been a priority for decades and Canada has had some success even though the overall numbers have not moved much. It is certainly true that Canada has expanded opportunities by signing free trade agreements with a number of countries. Canada- E.U. bilateral merchandise trade increased by 65.1 percent in the 6 years since the Comprehensive Economic and Trade Agreement (CETA)'s provisional application, although it's still too early to tell the impact of the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) on Canada's trade with the 11 Pacific nation that are parties to that mega-regional trade agreement.

However, for the past 20 years, the US has been the destination for generally around 75 percent of Canada's total exports, and for the previous 30 years was generally above 80 percent. Decreased reliance on the US is an

FIGURE 1: Per cent of Canadian exports destined for the U.S.



Source: Statistics Canada (2025).

improvement to be sure, but even if Canada were able to reduce its export dependence down to 70 percent or 60 percent, would it matter? Canada's dependence on the US would still be too high for comfort. Canadian policy-makers have to be clear on what Canada can reasonably achieve on reducing trade dependence from the US and be realistic about where three-quarters of its bread is buttered.

3. Inclusive trade

Inclusive trade has been the primary area of focus of Canada's trade policy under the current Liberal government – with decidedly mixed results. When the Liberals first formed government, they announced with much fanfare and preening a "progressive trade agenda" (Global Affairs Canada 2017). The government sought to address the "unequal distribution of the fruits of globalization" by including in trade agreements protections for labor, environmental standards, indigenous rights, gender equality, and human rights and ensure that they are "as much a part of the trade agreement as protections for investors" (Perrault 2020).

Some of the policy announcements were harmlessly performative – there were reports of Japanese negotiators giggling at Canada's insistence that the "Trans-Pacific Partnership" be renamed the "Comprehensive and Progressive Trans-Pacific Partnership" (Smith 2018) – but some Canadian experts have bemoaned the lack of substance in the progressive trade agenda.

In fact, there have always been doubts about the practical significance of including progressive language in free-trade deals and determining how such commitments could be enforced. Would Canada re-impose tariffs on countries that do not live up to their commitments on gender equality? Should other countries impose tariffs on Canada for Canada failing to provide clean drinking water in indigenous communities? As Dan Ciuriak, former deputy chief economist in Canada's Foreign Affairs Department has pointed out, "there is little evidence historically that such trade provisions have made a difference" (Curry 2017).

As foreign countries dismissed or rejected the "progressive elements" of trade deals with Canada (Hemmadi 2018), the government quietly abandoned the concept of "progressive trade" and eventually stopped using the word "progressive" altogether, although it still features conspicuously in the CPTPP (Smith 2019).

Under the Trudeau Liberal government, Canada's trade policy has been mostly reactive. Canada has successfully completed trade deals negotiated by the Conservatives with the E.U. (CETA), and with 10 Indo-Pacific nations (the CPTPP), has dealt with the renegotiation of NAFTA by Trump (resulting in the largely unchanged United States-Mexico-Canada Agreement (USMCA), and coped with a series of major trade disputes with China throughout the Meng Wanzhou/Huawei saga and the detention of the two Michaels. Muddling through is perhaps acceptable in ordinary times, but no longer. MLI

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