Canada’s Strategy for CUSMA Renewal

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1. Introduction

With the six-year review of CUSMA (Canada-United States-Mexico Free Trade Agreement) only two years away, the time is right for Canadian policymakers to start thinking about Canada’s optimal strategy for these discussions. This strategy will require an accurate assessment of U.S. objectives—complicated by uncertainty about the results of the November 5 election—and a clear view of Canadian objectives and vulnerabilities. Canada will also need to have a roadmap for how the discussions will play out—whether to deal with irritants first or hold concessions back, how closely to work with Mexico—and a plan to engage and then mobilize provinces and stakeholders, as was done so successfully in the original NAFTA renewal negotiations.

2. What will the political context be in the United States?

Two significant issues will likely dominate the political landscape in the U.S. presidential election in November: illegal migration and the strategic rivalry with China. While these issues were undoubtedly salient during the previous administration, they did not directly impinge on the free trade negotiations (with a few narrow exceptions, such as the prohibition on new trade deals with non-market economies). On China, both Canada and Mexico will need to convince the U.S. that they are not becoming back-door conduits for Chinese exporters trying to get around U.S. tariffs. This will be a particular challenge for Mexico, which has seen a boom in Chinese investment, but Canada will also need to be wary, as the U.S. has long viewed our trade countermeasures regime as lax. On illegal migration, the salience of the issue paradoxically could give the Mexicans a bargaining chip with the U.S., as their cooperation will be necessary for any meaningful reduction in numbers.

Regarding specific trade issues, the U.S. will undoubtedly come after Canada on dairy, seeking more access above the reasonably limited amount it received in the original negotiations and a more favourable administration of existing access. The Digital Services Tax Act will also be in USTR's (U.S. Trade Representative) crosshairs, given the lobbying heft of U.S. internet giants like Meta and Alphabet.

3. Will it matter whether it is Trump or Biden who wins?

A Trump presidency would be much more focused on reducing trade deficits and tariffs as a means to that end as Robert Lighthizer—who served as USTR in the Donald Trump Administration and will likely to be back in some capacity should Trump win—made crystal clear in an interview he gave to the Wall Street Journal on May 13, 2024. This will be a particular problem for Mexico, which has seen its trade surplus with the U.S. increase significantly since 2019, driven by autos.

Although Canada has also seen a rise in its trade surplus, this is primarily accounted for by Canada's energy exports to the U.S. whereas trade in autos is balanced. Trump will be hostile to Biden's green agenda; however, it is unlikely that he will unwind many of the subsidy measures, given their popularity in midwestern manufacturing states, which are crucial electoral battlegrounds. On issues such as energy security, supply chain security and preventing sensitive technology from reaching America's adversaries, there is likely to be little difference; both Biden and Trump are likely to build on what has already been done in this area by the Biden administration.

One area where we might see a significant difference between a Biden and Trump presidency is in its decision-making processes. Nothing can stop a U.S. administration from refusing to extend the CUSMA agreement while having annual reviews for ten years until the clock runs out. While a Biden administration would be content to wring whatever concessions they can from Canada and Mexico in exchange for the relative certainty that a new 16-year term would bring and then move on, it is not evident that a Trump administration would take the same view. With a potential Trump Presidency not ending until the end of 2028, Trump might prefer to spin the discussion out to keep up the pressure for more concessions and ensure continued Mexican cooperation on border issues. Admittedly, this would be better than Trump's repeated threats during the NAFTA renewal discussions to end NAFTA entirely: Trump is also unlikely to pull out of a trade agreement that he signed.

4. What should be Canada's overall objectives?

As with the original NAFTA renewal negotiations, Canada's objective should be to maintain its preferential access to the United States to maintain the integration of the two economies, particularly in industries such as autos. Given the potential chilling effect of protracted negotiations on investment, Canada must also try to extend the agreement in 2026 rather than having the negotiations drag out. This will likely require politically painful concessions on Canada's agricultural supply management policies, notably in dairy, to achieve.

5. What is Canada's best path to achieving these objectives?

First, Canada must move expeditiously to have the best shot at a timely renewal. Canada needs to engage early with the U.S. and Mexico—immediately after the U.S. elections—to agree on a negotiating process and a timeline.

Secondly, Canada needs to build up its broader bilateral relationship with the U.S. It will be vital that the U.S. sees Canada as a key partner that is helpful across a range of issues beyond trade, such as energy security, defence, cybersecurity and supply chain resilience. This will require Canada to significantly raise its game by meeting NATO targets for defence spending and reforming project approvals in the energy and minerals sectors (both of which should be high priorities for any Canadian government).

Thirdly, Canada must consider how it wants to deal with current trade irritants. One approach is to move quickly to deal with them before the USMCA discussions begin in earnest, to show good faith and to put the relationship on a better footing. However, there is a risk that the U.S. would simply pocket any unilateral concessions and be emboldened to seek more.

Fourthly, the Canadian government has to decide its stance towards Mexico. In the NAFTA renewal discussions, Mexico had a market-friendly government with which we were aligned on most issues—the exception being autos. However, the AMLO government in Mexico is much more economically nationalist, and this approach is likely to continue under AMLO's successor. Furthermore, the issues that concern all three countries are likely to be ones such as investment restrictions in Mexico's energy sector and rules of origin in the auto sector, where Canada's interests are much more closely aligned with the U.S. (the exception would be where the U.S. seeks something which impedes our ability to benefit from CPTPP). Thus, while Canada should ensure close relations with Mexico, Canada will be incentivized to line up with the U.S. in seeking concessions from Mexico.

Finally, Canada has to build a bureaucratic structure for the negotiations. This includes the following:

- Appointing a Chief Negotiator in GAC and building a negotiating team;
- Creating a mechanism for focused discussions with a range of stakeholders across Canada; and
- Setting up a group in the Canadian Embassy in Washington to coordinate our outreach to key players in the U.S., both in business and in politics.

This approach was adopted successfully during the NAFTA renewal negotiations, and a streamlined version would work well for the USMCA renewal discussions.

6. Conclusion

In any negotiation, two things ultimately matter: the parties' walk-away options and their discount rates, i.e., how impatient they are to conclude an agreement.

In the original NAFTA negotiations, Canada had much more to lose than the U.S. if the agreement was terminated. However, time was on Canada's side: Trump wanted a deal on one of his most significant signature initiatives before the U.S. midterms in November 2018 and before the exit of President Peña Nieto in that same month, whereas Canada could afford to wait. This time is different: USMCA will be a less salient issue in the U.S., and the Mexican administration will be in place until 2030. In Canada, we will want to see the potential threat to our most important trading relationship resolved expeditiously, and that means that the sooner we prepare and implement a strategy, the better.