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4 Recalibrating Canada's Trade and Economic Foreign Policy:

One China, Four China Approach

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CIPS, University of Ottawa
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Third Circle:

Calibrated Economic Engagement with China

(The "One China, Four Chinas" Approach)

The third circle, in effect, consists of a single but exceptionally large actor: the People's Republic of China. This circle reflects China's unique position as the world's second-largest economy and Canada's second-largest trading partner (after the United States), while at the same time recognizing that China is neither politically nor normatively aligned with Canada. China presents a set of challenges that are fundamentally different from those associated with partners in the first or second circles.

Relations with China are characterized by significant strategic and ideological frictions. China's authoritarian governance model, its highly contested human rights record, and its increasingly assertive foreign policy frequently conflict with Canadian values and interests. In recent years, bilateral relations have deteriorated sharply due to developments such as the Meng Wanzhou case and the detention of two Canadian citizens (2018–2020)[1], growing concerns regarding Chinese interference in Canada's domestic affairs, and persistent disagreements over issues including Hong Kong and Xinjiang.

For these reasons, China cannot be treated as a "normal" partner in the same way as Japan, or even Saudi Arabia. Nevertheless, given China's enormous economic weight and its central role in global supply chains, it is unrealistic to assume that Canada can pursue full decoupling or exclude China altogether from its diversification strategy.

[1] https://www.cbc.ca/news/meng-wanzhou-huawei-kovrig-spavor-1.6188472 (14,1,2026)

Canada therefore requires a multi-layered, nuanced, and segmented approach, one that allows for engagement with different "Chinas" across different domains. This is the logic underpinning the "Four Chinas" framework, introduced in this policy paper for the first time in the Canadian context. By conceptually disaggregating China into four distinct dimensions, Canada can better calibrate its engagement:

1. **China as a major economic and trade actor;**
2. **China as a powerful political and security actor;**
3. **China as a cultural–ideologic force;**
4. **China as a scientific and technological power.**

Through this analytical separation, Canada can maximize economic-trade gains from managed engagement with China (within the third circle) while minimizing the political and security risks that would arise from deeper, undifferentiated entanglement. This approach neither denies China's importance nor underestimates its risks; rather, it provides a structured and realistic framework for selective engagement consistent with Canada's long-term strategic interests.

China's Economic Attractiveness versus Political Challenges

1. China One: Economic / Trade China

On January 16, 2026, Canada and China reached a new trade agreement, aimed at easing tensions and lowering tariffs on electric vehicles and major agricultural exports, marking a shift after years of strained relations between the two countries.[2] China's economy offers substantial opportunities for Canadian exporters and investors, opportunities that cannot be easily ignored. In 2024, China accounted for approximately 3.8% of Canada's merchandise exports, valued at around CAD 29.9 billion. In the same year, Canada imported roughly CAD 87 billion worth of goods from China, underscoring China's significant share in Canada's overall imports.[3] Data from the first half of 2025 indicate a further increase in bilateral trade; for example, Canada–China merchandise trade reached approximately CAD 64.2 billion in the first half of 2025, representing growth compared to the previous year, with energy and mineral exports serving as the primary drivers of this increase.[4]

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[2] https://www.thenews.com.pk/latest/1388710-canada-china-trade-deal-all-you-need-to-know-about-the-new-agreement (21,1,2026)

[3] https://www.international.gc.ca/country-pays/china-chine/relations.aspx?lang=eng (21,1,2026)

[4] https://ccbc.com/ccbc-update/the-state-of-canada-china-trade-h1-2025/ (16,11,2025)

Canada exports a range of products to China, including wood, pulp, grains, oilseeds (during periods when restrictions are not in place), meat, and minerals, as well as certain services, most notably education. Tens of thousands of Chinese students study in Canada,[5] contributing billions of dollars to Canada's education sector and local economies. Although these flows declined during the COVID-19 period and amid diplomatic tensions, they remain economically significant.[6]

Many Canadian companies, from Bombardier to Shopify, have targeted China's vast consumer market. The scale of China's economy is such that even a small market share can translate into billions of dollars in sales.[7] Prior to 2019, for example, China was one of Canada's most important markets for canola and pork.[8] Diplomatic tensions subsequently led to temporary import bans that inflicted hundreds of millions of dollars in losses on Canadian farmers. These restrictions were lifted in 2022, but the episode clearly demonstrated that China represents both a major opportunity and a major risk for Canada.

From a diversification perspective, China's economic growth can help offset downturns in other markets. China's approximately 5% economic growth in 2025 suggests that, despite a slowdown compared to earlier decades, it remains one of the principal engines of global economic growth. This growth, however, is increasingly quality-oriented and state-managed, rather than the explosive expansion of previous decades, with the Chinese government seeking to anchor it in domestic consumption, advanced technologies, and the green transition.[9] Demand in China for commodities, high-quality food products, and services such as tourism is therefore expected to remain strong.

Canada's tourism and education sectors benefited enormously during peak periods of Chinese arrivals. In 2019, more than 708,000 Chinese tourists visited Canada, making China one of Canada's most important long-haul tourism markets.[10] In the same year, Chinese nationals constituted the second-largest group of international students in Canada, with approximately 140,537 study-permit holders, second only to India.[11] Official statistics show that in 2023, travel from Asia to Canada remained below 2019 levels due to the lingering

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[5] https://www.international.gc.ca/education/report-rapport/impact-2022/index.aspx?lang=eng (12,1,2025)

[6] https://www150.statcan.gc.ca/n1/pub/13-605-x/13-605-x2023001-eng.htm (4,10,2025)

[7] https://www.international.gc.ca/country-pays/china-chine/relations.aspx?lang=eng (14,1,2026)

[8] https://www150.statcan.gc.ca/n1/daily-quotidien/190305/dq190305b-eng.htm (14,1,2026)

[9] https://www.imf.org/en/news/articles/2025/12/10/pr-25415-china-imf-staff-completes-2025-article-iv-mission-to-the-peoples-republic-of-china (16,12,2025)

[10] https://archives.destinationcanada.com/en/markets/china (16,12,2025)

[11] https://www.canada.ca/en/immigration-refugees-citizenship/corporate/transparency/committees/cimm-feb-28-2024/international-student-program-at-a-glance.html (23,5,2025)

effects of COVID-19 and reduced outbound travel from China. Nevertheless, the recovery trend is evident: according to Statistics Canada, approximately 206,275 visitors from China entered Canada in August 2023[12]. As bilateral relations stabilize and post-pandemic conditions normalize, these figures could rise again, injecting renewed vitality into Canada's local and national economies.

2. China Two: Political–Security China

The Chinese government has demonstrated that it is willing to employ economic coercion as a response to political disagreements:

- Australia faced sweeping import bans after calling for an investigation into the origins of COVID-19;
- Canada, following the arrest of Huawei's Chief Financial Officer, was subjected to canola import bans and the arbitrary detention of two Canadian citizens;
- Other countries have likewise experienced pressure after meetings with the Dalai Lama or criticism of China's human rights record.

Accordingly, any Canadian effort to expand economic relations with China must incorporate mechanisms to reduce vulnerability. Examples of such risk-management measures include:

- Diversification within the Chinese market (selling to multiple buyers rather than relying on a single state-owned enterprise);
- Identifying alternative markets for critical exports;
- Building domestic capacity to withstand informal or unofficial sanctions.

Canada's Indo-Pacific Strategy explicitly acknowledges this duality. On the one hand, it recognizes that *"China's size and influence make cooperation necessary to address global challenges, and its economy presents significant opportunities for Canadian exporters"*; on the other hand, it affirms that *"Canada will challenge China when it undermines international rules or Canadian interests."*[13]

This is precisely the dual-track approach Canada must adopt: expanding trade while simultaneously safeguarding national interests and mitigating political risk.

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[12] https://www150.statcan.gc.ca/n1/pub/12-581-x/2023001/sec19-eng.htm (22,7,2025)

[13] https://www.international.gc.ca/transparency-transparence/indo-pacific-indo-pacifique/index.aspx?lang=eng (6,1,2026)

From a foreign-policy perspective, Canada must remain firmly committed to its values and security imperatives. In coordination with its allies, Canada should continue to push back against China's coercive behaviors, from the militarization of the South China Sea to unfair trade practices. Domestically, Canada must protect itself by strengthening counter-foreign-interference legislation, enhancing oversight of, and where necessary blocking, investments by Chinese state-linked firms in sensitive sectors (as illustrated by Canada's 2022 decision to prohibit Chinese investment in critical minerals projects due to national security concerns[14]), and allocating resources to bolster cybersecurity and counter state-linked espionage.

These measures imply that even if Canadian companies engage in trade with China, the Canadian state must ensure that critical infrastructure and sensitive sectors remain insulated from Chinese influence or control.

Such protection may include:

- Stricter export controls on sensitive technologies;
- Rigorous screening of research collaborations;
- Intelligence-sharing with allies regarding China-related activities.

In short, in the political and security domain, Canada should engage China as a security competitor, employing highly calibrated and diplomatic actions aligned with G7 and NATO assessments, while keeping economic and commercial engagement as the primary, but carefully managed, track.

3. China Three: Cultural-Ideologic Dimension

The cultural–ideologic dimension refers to the values and social systems of the two countries. In this sphere, Canada must acknowledge that Canadian and Chinese social values differ fundamentally, particularly with regard to individual freedoms, democracy, and human rights. It would therefore be misguided to assume that economic engagement alone will rapidly lead to China's democratization; experience over past decades clearly contradicts such an assumption.

[14] https://www.canada.ca/en/innovation-science-economic-development/news/2022/10/government-of-canada-orders-the-divestiture-of-investments-by-foreign-companies-in-canadian-critical-mineral-companies.html (12,9,2025)

At the same time, it is essential to distinguish between the Chinese Communist Party (CCP) and the Chinese people. Over 1.8 million Canadian residents are of Chinese origin, and on December 31, 2024, approximately 100,000 Chinese citizens held valid study permits for studying at a Canadian educational institution for 6 months or longer. Mandarin is Canada's third most spoken language after English and French, and immigrants born in China (including the Hong Kong Special Administrative Region) form one of the largest groups within Canada's immigrant population. Tourism flows and ongoing cultural exchanges enrich bilateral linkages.[15] Moreover, cultural, academic, artistic, and civil-society ties between the peoples of the two countries, if carefully managed, can foster mutual understanding and reduce the risk of misperception or unnecessary tension.

Canada's Indo-Pacific Strategy explicitly emphasizes this point, noting that *"the people of Canada and China are the cornerstone of our relationship"* and that Canada must *"distinguish between the actions of the Chinese government and the Chinese people."*[16] Accordingly, cultural engagement should remain open and sustained, encompassing the following areas:

- Encouraging educational and academic exchanges;
- Continuing to welcome Chinese students (while maintaining reasonable security oversight);
- Promoting Canadian values through public diplomacy, including support for Canadian cultural and media content in Mandarin;
- Expanding Canada–China academic dialogues on shared global challenges, such as climate change.

Such cultural engagement is inherently a long-term process, an opportunity to build understanding and trust over decades, and is fully consistent with Canadian values. At the same time, Canada must remain vigilant to ensure that these interactions are not exploited by the Chinese state, for example for state propaganda purposes or for interference within Canadian society. It is therefore essential that Canada:

- Protect the freedom and security of Chinese-Canadian communities;
- Ensure that no individual in Canada is subject to intimidation, surveillance, or political pressure by a foreign government.

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[15] https://www.international.gc.ca/country-pays/china-chine/relations.aspx?lang=eng (5,1,2026)

[16] https://www.international.gc.ca/transparency-transparence/assets/pdfs/indo-pacific-indo-pacifique/indo-pacific-indo-pacifique-en.pdf (14,9, 2025)

In this way, Canada can sustain meaningful people-to-people engagement with China while safeguarding democratic integrity and social cohesion at home.

4. China Four: Scientific and Technologic China

China today is a scientific and technological superpower. It has made massive investments in research and development and is on a trajectory to become a dominant global force in areas such as artificial intelligence, biotechnology, quantum computing, and space technologies.[17] This reality presents Canada with both a competitive challenge and selective opportunities for cooperation.

For Canada, the primary concern in engaging with China in this domain is national security. A clear distinction must therefore be drawn between sensitive and non-sensitive technologies. Canada must not allow the transfer of sensitive Canadian technologies to China, particularly those that could enhance China's military capabilities or state surveillance systems. Within this framework, Canada's decision to exclude Huawei from its 5G networks appears to have been prudent. Canada has also strengthened oversight of research collaborations to prevent intellectual property theft or unintended technology transfer. These measures, and similar ones, should not only continue but be further reinforced.

At the same time, there are domains in which scientific cooperation with China is both necessary for Canada's global interests and largely free of security sensitivities, including:

- Global public health: joint research on pandemics, where Chinese data and cooperation are essential;
- Environment and climate change: given China's major role in global greenhouse gas emissions and its control over critical environmental data.

Cooperation in such areas, particularly through multilateral frameworks, serves the interests of all countries. As Canada's Indo-Pacific Strategy explicitly states, Canada will work with China to identify shared solutions on issues such as climate change, biodiversity loss, global health, and nuclear non-proliferation.[18] This may include cooperation under

[17] https://www.atlanticcouncil.org/content-series/strategic-insights-memos/assessing-chinas-ai-development-and-forecasting-its-future-tech-priorities/ (7,10,2025)

[18] https://www.international.gc.ca/transparency-transparence/assets/pdfs/indo-pacific-indo-pacifique/indo-pacific-indo-pacifique-en.pdf (14,11,2025)

frameworks such as the Paris Agreement, or participation in World Health Organization (WHO) projects aimed at disease control, irrespective of existing political disagreements.

With regard to the competitive dimension of technology, in the contemporary international system, given the divergent political and security approaches of Canada and China, technological competition with China is unavoidable. Accordingly, Canada should increase investment in domestic innovation and deepen cooperation with its allies, particularly Australia and Japan, which are identified in Circle One of this policy paper, to ensure that it does not fall behind China in critical and sensitive technological domains.

It should also be recognized that technological engagement with China does not always imply partnership or integration, but may simply involve learning, monitoring, and maintaining channels of interaction. For example, examining China's progress in electric vehicle batteries (as mentioned in the China-Canada Trade Deal in January 2026), or tracking its rapid advances in artificial intelligence, enables Canada to better calibrate and refine its own national science and technology strategies.

Moreover, scientific engagement can function as an informal diplomatic channel. As demonstrated during the Cold War, American and Soviet scientists maintained scientific exchanges even amid severe political tensions.[19] In this sense, preserving academic dialogue with China, while applying caution and robust protective frameworks, can be both valuable and constructive.

Implementing the "One China, Four China" Approach

Given the complexity of engaging simultaneously with the "four Chinas," Canada's strategy in Circle Three should be guided by the following principles:

• Maximizing Economically Beneficial Engagement for Canada

Canada should encourage its exporters to take advantage of opportunities in the Chinese market, while deploying risk-mitigation instruments, such as Export Development Canada (EDC) export insurance, to reduce exposure. In addition, Canada could cautiously resume official economic dialogues with China at the technical level, which were suspended after 2018, strictly for trade facilitation purposes. While a Canada–China free trade agreement is politically unrealistic under current conditions, sector-specific arrangements or targeted

[19] Olga Krasnyak (2019), "How U.S.-Soviet Scientific and Technical Exchanges Helped End the Cold War,"Available at: How U.S.-Soviet Scientific and Technical Exchanges Helped End the Cold War | American Diplomacy Est 1996 (23,12,2025)

cooperation, for example, updating the *Canada–China Film Co-production Agreement* or concluding a *tourism cooperation agreement*, could be explored.

• Minimizing Political Entanglement

Since the core objective in Circle Three is managed economic engagement, Canada should not pursue any form of comprehensive strategic partnership or deep political alignment with Beijing under present circumstances. High-level political contacts should be pragmatic. Canada should not offer political or symbolic concessions to China in exchange for economic gains, concessions that rarely deliver the promised returns. Accordingly, Canada must ring-fence and safeguard its values: there should be no retreat on human rights, and no compromise on strategic alliances. Even if such positions provoke dissatisfaction in Beijing, Canada must continue to raise issues such as human rights violations in Xinjiang and the erosion of freedoms in Hong Kong. These are principled positions and should not be treated as negotiable assets.

• Fortifying Defenses

Canada must strengthen its domestic laws and institutions to mitigate the negative externalities of engagement with China. This includes:

- Updating the Investment Canada Act to apply stricter screening of investments linked to the Chinese state;
- Enhancing the capacity of the Canadian Security Intelligence Service (CSIS) and the Royal Canadian Mounted Police (RCMP) to counter foreign interference;
- Protecting Chinese-Canadian communities from intimidation, coercion, or external political influence;
- Cooperating with social media platforms to counter disinformation and influence operations.

A core component of the Indo-Pacific Strategy also emphasizes strengthening Canada's analytical and cognitive capacity on China, including investments in research, training China-specialist diplomats, and expanding Mandarin language education,[20] so that Canada can engage China from a position of knowledge, confidence, and strategic awareness.

• Working Multilaterally

[20] https://www.international.gc.ca/transparency-transparence/assets/pdfs/indo-pacific-indo-pacifique/indo-pacific-indo-pacifique-en.pdf (8,12,2025)

While Canada's unilateral leverage over China's political and security behavior is limited, its influence increases significantly when acting alongside the G7, the European Union, ASEAN, and other partners. Key steps in this regard include:

- Coordinating with allies on trade and regulatory standards;
- Joining collective legal challenges at the WTO when China violates trade rules;
- Shaping joint positions on core security and governance issues.

At the same time, Canada can continue constructive multilateral cooperation with China where interests align. A prominent example is the 2022 United Nations Biodiversity Conference (COP15), hosted by Canada in Montreal with China serving as a co-chair, demonstrating that cooperation is possible even amid broader tensions.[21]

In parallel with these measures, Canada should continue to diversify critical supply chains away from excessive dependence on China, a process that will be advanced in part through Circle Two, particularly by deepening engagement with ASEAN and other alternative producers.

Likely U.S. Reaction

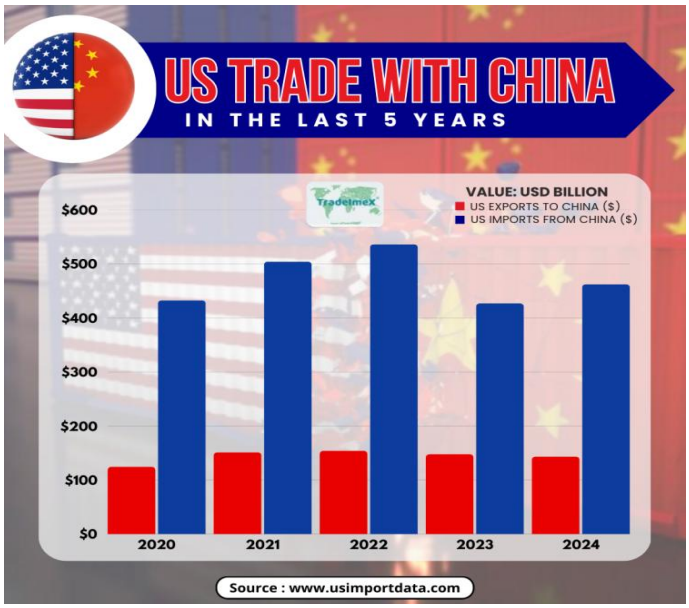
This balanced approach toward China is also essential for preserving Canada's most important foreign-policy relationship, its relationship with the United States. Even in the era of tariff war, Washington expects Canada to remain aligned on strategic China-related issues, an expectation that has largely been met, as reflected in Canada's decision to ban Huawei from its 5G networks and to condemn Chinese interference in Canada's domestic affairs.

Where U.S. concern could arise is if Canada were to expand its economic relations with China in ways that undermine collective allied efforts. For example, if Canada were to pursue a bilateral free trade agreement with China that effectively provides China with a "backdoor" into the North American market, Washington would strongly object.

The approach proposed here does not contemplate such actions, and the domestic political environment in Canada would not support them in any case. The proposed engagement is limited to the sale of Canadian goods and the maintenance of dialogue channels on global issues, an approach that mirrors U.S. practice itself. The United States maintains extensive trade with China and continues high-level dialogues despite strategic rivalry.

[21] https://www.unep.org/news-and-stories/story/cop15-ends-landmark-biodiversity-agreement (9,9,2025)

Figure 5: US-China Trade (2020-2024)



As long as Canada remains aligned with the United States and its allies on core strategic issues, Washington is likely to accept, or even appreciate, Canada's careful and balanced role. For instance, if Canada can serve as a mediator or facilitator of dialogue in specific areas such as climate change or global health, this could reinforce the broader Western strategy toward China.

That said, the United States will closely monitor Canada's China policy. Accordingly, while exercising foreign-policy autonomy, Canada must maintain full transparency with Washington and with its strategic partners in the first circle, as well as with the European Union, regarding its objectives and red lines. In practice, the success of Circle Three requires walking a fine line: pursuing economic engagement without weakening national security or allied commitments. This is difficult, but not impossible.

Several U.S. allies, including Japan and Germany, have adopted precisely this dual approach: trading with China while actively managing strategic risks. Japan, in particular, offers a useful model for Canada. Despite deep commercial ties with China, Japan is among the most proactive countries globally in countering China's threatening security behavior. Canada could work closely with Japan and other partners to share best practices in risk management and strategic resilience.

Synthesis of Circle Three

China occupies a distinct and sui generis position in the recalibration of Canada's foreign policy. It is neither a full partner nor a full adversary; rather, it is simultaneously a partner in certain domains, a competitor in others, and a systemic challenger in yet others, an approach often described as one of "competition, cooperation, and challenge at the same time." By disaggregating the concept of "China" into four analytical dimensions and designing differentiated policies for each, Canada can pursue a strategy of smart engagement with China that is both realistic and resilient:

- engaging in trade and investment where this clearly serves Canadian interests and contributes to diversification in the context of reduced or uncertain access to the U.S. market;
- avoiding strategic dependence on China in critical sectors; and
- maintaining firm adherence to Canadian values and allied commitments in the face of any hostile behavior or violations of international law.

This calibrated and carefully sequenced Third Circle strategy ensures that, even if the full realization of the First or Second Circles requires time, Canada can still maintain a managed, controlled, and interest-based relationship with the world's second-largest economy. Such an approach allows Canada to benefit from access to Chinese markets without drifting into China's sphere of influence. The balance is inherently difficult, but under current conditions it represents the only pragmatic pathway for managing the economic pressures generated by U.S.-led trade conflicts and for preventing broader economic disruption.

U.S. Reactions and Managing the Transition Period

One of the critical dimensions of implementing the three-circle foreign policy framework is anticipating and managing the reaction of the United States, given that Canada's economy and security still remain deeply intertwined with those of the U.S. As Canada pivots toward new partners, Washington will undoubtedly monitor these developments closely. Based on the preceding analysis, a spectrum of likely U.S. responses can be anticipated as follows:

1. Support and Reassurance (Circles One and Two)

In initiatives involving Japan, Australia, and, most likely, many engagements with Southeast Asia and the Gulf states, the U.S. reaction is expected to be positive or neutral. These moves are broadly aligned with American interests:

- strengthening the alliance network (Circle One), and
- providing stable, non-Chinese alternatives in strategically important regions of the world (Circle Two).

For example, if Canada succeeds in attracting major investments from the United Arab Emirates or other Gulf countries, or in expanding its trade with India and ASEAN, the United States will see the emergence of a stronger and more resilient Canadian economy, one that is less dependent on U.S. support while simultaneously contributing to shared strategic objectives in the Indo-Pacific and the Middle East.

As David Moscrop has noted in *TIME* magazine, Canada's turn toward such pragmatic partnerships represents a rational response to the "global economic environment shaped by the challenges of the Trump era."[22] It is also noteworthy that even at the height of NAFTA-related tensions, some U.S. officials privately encouraged Canada to diversify its trade portfolio in order to enhance its bargaining power.[23]

A more diversified Canada is a less vulnerable Canada, and therefore a more secure neighbor for the United States. Accordingly, with respect to Circles One and Two, aside from routine questions or the need for initial coordination, such as ensuring that technological cooperation with Gulf partners does not result in the unintended transfer of U.S.-controlled technologies, serious friction with Washington is unlikely.

2. Cautious Monitoring (Circle Three – Economic Engagement with China)

With respect to China, the U.S. reaction is likely to be mixed and cautious. The United States welcomes Canada's firm stance on security issues (such as the ban on Huawei and the screening of Chinese investments), but it will closely monitor Canada's commercial dealings with China. If Canada merely maintains its current level of trade with China, or increases it in a limited and calibrated manner, the United States is unlikely to object, particularly given that U.S.–China trade itself remains far more extensive, and Washington recognizes that its allies inevitably trade with China.

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[22] https://time.com/7337391/canada-carney-economy-trade-trump/ (16,12,2025)

[23] https://www.piie.com/microsites/2025/future-usmca (20,1,2026)

However, if the perception emerges that Canada is, even inadvertently, undermining U.S. pressure on China, for example by facilitating the circumvention of U.S. tariffs or export controls, this would trigger serious concern and a strong reaction from Washington.

To prevent such a scenario, Canada should take the following proactive steps:

- Strict enforcement of re-export regulations to prevent Chinese goods from transiting through Canada into the United States for the purpose of evading tariffs or trade remedies.
- Close consultation with the United States on major transactions; for example, if a Chinese firm seeks to invest in a Canadian critical minerals project, informal advance notification to U.S. counterparts would be a prudent and confidence-building measure.

Overall, as long as Canada's engagement with China remains calibrated, transparent, and aligned with the broader posture of its allies, the United States is likely to regard it as reasonable and acceptable. Indeed, the Indo-Pacific strategies of many U.S. allies are based on the same logic: continued trade with China alongside firm pushback in other domains.[24]

The scenario Canada must avoid is one in which the United States is considering new sanctions against China while Canada opportunistically expands its exports to fill the resulting gap. Such behavior could be perceived as profiting at the expense of an ally. Given Canada's values-based foreign policy and its established record of coordination on sanctions regimes (for example, in the case of Russia), such conduct is unlikely. With China as well, Canada should adhere to the same pattern of coordination on major measures.

3. NAFTA / USMCA Considerations

One area requiring particularly careful management is the interaction between Canada's new initiatives under the three proposed circles and the USMCA (the successor to NAFTA). Notably, Article 32.10 of the USMCA contains a clause allowing any party to withdraw from the agreement if another member concludes a free trade agreement with a "non-market

[24] https://www.uscc.gov/sites/default/files/2024-11/Chapter_1--U.S.-China_Economics_and_Trade_Relations_Year_in_Review.pdf (9,11,2025)

country",[25] a term widely understood to refer to China. This provision was included at U.S. insistence and effectively constitutes a veto over any Canada–China free trade agreement.

At present, prudence dictates that Canada should have no intention of activating such a scenario, as the clause clearly reflects the high sensitivity of the United States on this issue. By contrast, the expansion of Canada's relations with other countries that the United States does not classify as "non-market economies" poses no such problem. In fact, the United States has no objection to Canada's participation in the CPTPP, nor to the prospect of a Canada–ASEAN free trade agreement. The United States itself may, in time, re-engage with Asian trade frameworks or launch new initiatives; Canada's activity in these areas would therefore complement U.S. policy rather than conflict with it.

Policy Recommendations

Canada stands at a critical inflection point in its foreign policy, one that compels us to confront difficult realities. Canada's economic security can no longer rest on the assumption of permanent goodwill and enduring stability in our most important trading relationship. The tariff war initiated in 2018 under the Trump administration's "America First" and "Make America Great Again" agenda, and reaching its peak in 2024, served as a stark warning: even Canada's closest ally can, under a particular type of political leadership, disrupt the status quo and impose heavy economic costs on Canada in pursuit of domestic political gains.

To be sure, Donald Trump was not the first U.S. president to exert pressure on Canada. From the long-standing softwood lumber disputes of the 1980s to the protectionist shocks of the Nixon era, history repeatedly demonstrates that Canadian interests and U.S. domestic politics periodically collide, and Trump will not be the last. The persistence of the MAGA movement and the possibility of a return or repetition of populist nationalism in U.S. politics underscore a clear lesson: Canada must plan for worst-case scenarios, even while hoping for the best.

This policy paper has outlined a comprehensive three-circle framework for a bolder, more diversified, and forward-looking Canadian foreign policy, one aimed at safeguarding Canada's economic future in a world marked by deep uncertainty. This approach does not advocate a rupture with traditional partners; rather, it is grounded in the intelligent expansion of options, the reduction of vulnerabilities, and the strengthening of national

[25] https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cusma-aceum/text-texte/32.aspx?lang=eng (6,11,2025)

resilience. It charts a course that allows Canada to remain proactive and prepared, rather than merely reactive, in an increasingly unstable global environment.

In concluding, it should be emphasized that to implement this strategy, the Government of Canada (and the policy advisors to whom this policy paper is addressed) should consider the following practical steps:

1) Establish a Diversification Task Force

A high-level task force should be created under Global Affairs Canada (GAC) and the Department of Finance or other relevant departments to lead and coordinate the three-circle framework. This task force should set measurable targets, such as "increase exports to Circle One and Circle Two countries by X percent by 2030" or "attract Y billions of dollars in non-U.S. foreign investment over the next five to ten years", ensure interdepartmental coordination, and report regularly to the Prime Minister and Cabinet so that whole-of-government alignment is maintained. To enhance credibility and effectiveness, the presence of representatives from provincial governments on this task force is essential, because, in practice, trade diversification is often achieved through provincial export-promotion programs.

2) Intensify Trade Negotiations and Agreements

Ongoing negotiations, especially the Canada–ASEAN Free Trade Agreement and the Canada–Indonesia Comprehensive Economic Partnership Agreement (CEPA), should be accelerated through greater resource allocation, with the objective of concluding high-quality agreements in the 2027–2030 period. At the same time, new negotiating tracks should be pursued. In addition, Canada should revisit the feasibility of a Canada–Gulf Cooperation Council (GCC) trade agreement; negotiations were previously stalled, but the warming of relations with Saudi Arabia and the United Arab Emirates creates an opportunity to return to this file. The Canada–UAE Comprehensive Economic Partnership Agreement (CEPA) could be a constructive starting point and serve as a platform for a broader agreement with the GCC. Finally, existing agreements should be modernized and fully implemented; for instance, ensuring the full ratification of CETA by the remaining EU member states, since Europe remains a "key existing partner" that should not be neglected, even if this policy paper's focus is on other regions.

3) Trade Promotion and Support for Small and Medium-Sized Enterprises (SMEs)

A dedicated "Export to Diversified Markets" Program should be launched for Canadian SMEs, with the objective of reducing the risks associated with entering markets in Circles Two and Three. This program could include the following components:

- Increasing the budget of Export Development Canada (EDC) to expand risk coverage in higher-risk markets;
- Providing grants or cost-sharing mechanisms for trade missions or e-commerce initiatives targeting markets in Asia, Central Asia, the Middle East, Africa, and Latin America (although Latin America and Africa are not examined in detail in this paper, diversification should also encompass renewed and robust engagement with these regions, perhaps as a "Circle 2.5", given their significant growth potential).

The overarching objective is to lower the barriers for Canadian firms entering non-U.S. markets and to facilitate a gradual, managed exit gradually from the perceived "safe zone" of the U.S. market.

4) Leveraging Immigration Policy and Diaspora Networks

Canada's demographic diversity constitutes a strategic asset for building external economic linkages. For example, Canada's Indian, Chinese-origin and Arab communities can serve as effective bridges for engagement with India, China and Gulf Countries, respectively (and other diaspora communities can play similar roles). The government should actively collaborate with these communities and encourage them to identify trade and investment opportunities in their regions of origin. Practical measures could include, but are not limited to:

- Establishing advisory councils composed of business leaders from diaspora communities to provide guidance to Global Affairs Canada on market strategies beyond North America;
- Facilitating targeted immigration pathways for idea owners, traders, investors, and students from countries across the three circles.

Every international student or entrepreneur from ASEAN, the Gulf states, or other regions who has a positive experience in Canada, whether they eventually return home or remain, can become an informal ambassador for Canadian trade and investment.

Accordingly, educational exchanges, particularly with countries in Circles One and Two, should be expanded. For example, Canada could increase the number of scholarships awarded to students from ASEAN countries in line with the commitments outlined in the Indo-Pacific Strategy.

5. Protecting and Enhancing Domestic Competitiveness

Diversification will succeed only if Canadian industries remain competitive in terms of quality and innovation. Accordingly, the government must complement trade and foreign policy initiatives with domestic policies aimed at boosting productivity in the long term, including:

- Investment in infrastructure (ports, transportation networks, and coastal export corridors to facilitate shipments to Asia);
- Investment in technology and skills (so that Canadian exporters can produce the goods and services demanded by new markets);
- Strengthening strategic sectors such as critical minerals (for example, accelerating mining permitting processes so that Canada can meet the battery supply needs of Japan and Korea).

The 2025 federal budget could have included a dedicated package entitled "Competitiveness for Diversification," directly aligned with this strategy.

6. Maintaining a Delicate Balance with the United States

As emphasized throughout, the United States retains the capacity to disrupt any diversification strategy pursued by Canada. Therefore, sustained diplomatic engagement with Washington is essential. Should the United States seek to exert additional pressure on Canada to advance political objectives, Canada should also be prepared to adopt alternative approaches. Such approaches could include inviting the United States to participate in selected initiatives, for example, encouraging U.S. firms to take part in Canada-led infrastructure projects in Asia (like the approach Japan has at times adopted in its own projects involving the United States).

7. Regular Review and Scenario-Based Planning

Given the inherent unpredictability of global politics, Canada must institutionalize strategic intelligence within its foreign and trade policy framework. This requires conducting annual reviews of the performance of foreign and trade policy across each of the proposed circles, as well as implementing scenario-based planning exercises for all plausible futures.

For instance, if one plausible scenario is that the 2028 U.S. presidential election results in a renewed return of the "MAGA" agenda, Canada must already have a contingency plan in place to accelerate certain partnerships, such as rapidly deepening trade relations with the United Kingdom and the European Union. Although these regions were not central to this report due to the ramifications of the war in Ukraine, they nevertheless remain important and stabilizing partners.

Conversely, if the United States were to be governed by a strongly pro–free trade administration, Canada could once again place temporary and tactical emphasis on North American trade, strictly for the purpose of compensating for the economic losses incurred as a result of the post-2024 tariff war.

8. Calculating the Political and Economic Costs of Diversification

Although trade and strategic diversification can enhance Canada's long-term economic security and geopolitical resilience, this path is not without costs. Ignoring the short- and medium-term costs of diversification can lead to overly optimistic assessments and, ultimately, implementation failures. A realistic strategy must therefore explicitly identify and manage the political, economic, and institutional costs of this transition alongside its benefits. These costs can be organized into three main categories:

8-1. Infrastructure and Physical Investment Costs

Canada's trade diversification, particularly toward China, Australia, Japan, the Asia–Pacific, the Middle East, Central Asia, East Asia, and other distant markets, requires a substantial reconfiguration of the country's physical infrastructure. Historically, Canada's economy has been structured around deep integration with the United States, and its infrastructure, railways, highways, ports, and energy terminals, have largely been oriented southward toward the U.S. market. A pivot toward non-U.S. markets challenges this entrenched economic geography.

In practical terms, this entails large-scale investments in:

- the expansion and modernization of West and East Coast ports (notably Vancouver, Prince Rupert, and Halifax) to increase export capacity to Asia and Australia;
- the development of LNG infrastructure and energy export corridors to non-U.S. markets;
- improvements in logistics networks, warehousing, and multimodal transportation to reduce costs along longer supply routes.

These investments typically require billions of dollars, take considerable time to complete, and are often accompanied by domestic political challenges, including environmental concerns, Indigenous rights, and federal–provincial disputes. Diversification is therefore not a low-cost option, but rather a national investment project that requires political consensus and sustained financing.

8.2. Diplomatic, Institutional, and Human-Capacity Costs

Effective diversification does not occur through markets and the private sector alone; it is highly dependent on state capacity. A sustained presence in new markets requires the expansion and deepening of Canada's diplomatic and commercial footprint in target regions. This generates significant costs, including:

- the expansion or strengthening of Canada's diplomatic and trade missions in Asia, ASEAN, the Middle East, and other emerging regions;
- the training and deployment of diplomats, trade negotiators, and regional specialists with linguistic, cultural, and economic expertise;
- the reinforcement of institutions such as the Trade Commissioner Service (TCS), Export Development Canada (EDC), and other trade policy delivery mechanisms.

While these costs are often less visible than infrastructure expenditures, they are critical to the success of any diversification strategy. Without sufficient human and institutional capacity, trade agreements will not translate into tangible outcomes for Canadian firms. In this sense, diversification requires a more capable and proactive state, not a minimalist one.

8.3. Geopolitical Costs and Friction with the United States

Perhaps the most sensitive cost of diversification is the increased risk of short-term friction with the United States. Canada's economy remains deeply intertwined with that of the U.S., and any effort to reduce dependence or create alternative options may be viewed in Washington with suspicion or concern, particularly during periods of U.S. protectionist or nationalist policy orientations.

Such friction may manifest in several ways:

- political or media pressure targeting Canada's independent trade policies;
- instrumental use of USMCA mechanisms to constrain Canadian initiatives;
- or even short-term retaliatory measures, such as increasing tariffs, regulatory delays, or informal restrictions.

While these costs are not necessarily permanent or structural, they can impose significant short-term burdens on specific Canadian industries or provinces.

Conclusion and Assessment of Implementation

To assess the effectiveness of the three-circle framework and to ensure the practical realization of Canada's economic diversification objectives, it is essential to define a set of quantitative, measurable, and reportable indicators. In the absence of such benchmarks, diversification risks remaining a largely discursive ambition, with no reliable means of evaluating real progress. Accordingly, this policy paper proposes a set of Key Performance Indicators (KPIs) that should be monitored on a regular and annual basis.

The first and most fundamental indicator is reducing Canada's trade dependence on the United States. Within this framework, the objective is to lower the U.S. share of Canada's total trade from the current level of approximately 75 percent to around 50–60 percent by 2030. Over a longer time horizon beyond 2030, a gradual move toward a range of roughly 25–30 percent may be considered as a strategic end goal. This indicator directly reflects the extent to which high-risk concentration is being reduced and the structural resilience of the Canadian economy strengthened.

The second indicator concerns growth in Canadian exports to First Circle and Second Circle countries. Specifically, exports to these countries should increase by at least 30–40 percent by 2030 as a concrete quantitative target; the share of Japan, Australia, ASEAN+3, Persian Gulf Countries, and other emerging economies in Canada's overall exports should be monitored annually to determine whether a meaningful shift in the geographic composition of exports is taking place.

The third key indicator is the expansion of non-U.S. foreign direct investment (FDI) in the Canadian economy. This includes increasing the share of non-U.S. FDI in total inward investment and attracting tens of billions of dollars in new investment from China (Economic/Trade China), the regions such as ASEAN+3, the Gulf states, Japan, and Australia by 2030. This indicator captures whether Canada has been successful in diversifying its sources of capital and reducing financial dependence on a single country.

The fourth indicator relates to the operationalization of trade agreements. The success of the three-circle framework should be measured not merely by the launch of negotiations, but by the conclusion and effective implementation of free trade agreements or comprehensive economic partnerships (FTAs and CEPAs). In this regard, finalizing and bringing into force at least 10 to 20 new agreements by 2030, such as with ASEAN+3 countries, and other Gulf countries, should be a core target. A complementary indicator in this domain is the actual utilization rate of these agreements by Canadian firms, which serves as a measure of their practical effectiveness.

The fifth indicator focuses on the level of participation by small and medium-sized enterprises (SMEs) in non-U.S. markets. An increase in the number of Canadian SMEs exporting to Circle Two and Circle Three markets, along with a clearly defined annual growth rate, for example, a 10 percent increase in the number of exporting firms, would signal that diversification is deepening and becoming more broadly embedded across the Canadian economy.

Finally, a set of institutional and capacity-building indicators should be taken into account. These include increasing the number of active trade offices, economic diplomats, and targeted trade missions in priority regions, as well as reducing the time required for firms to access support services provided by institutions such as Export Development Canada (EDC) and the Trade Commissioner Service (TCS) in new markets. Improvements in these indicators would demonstrate the government's institutional capacity to provide effective, hands-on support for diversification efforts.

These indicators should be reviewed on an annual basis and incorporated into the government's formal reporting to Parliament and the Cabinet. The success of the three-circle framework should be measured not by symbolic agreements or rhetorical commitments, but by tangible changes in trade patterns, investment flows, and Canada's overall economic resilience. Only through such a framework can diversification move from a policy slogan to a durable economic reality.

Implementing the steps outlined within the proposed three-circle foreign policy framework will require political courage and strategic foresight from Canadian leadership. Undoubtedly, criticisms will arise. Some will argue that even limited engagement with authoritarian governments such as Saudi Arabia or China carries excessive costs; others will express concern about increased pressure from the United States. Political leadership, however, must articulate the logic of this path with clarity and confidence.

Canada is not in confrontation with any partner; but it has learned that alliances are inherently vulnerable and therefore seeks to ensure that it is never left alone in the future. The world must be told clearly that Canada remains a trading nation, committed to multilateralism and shared values, but no longer naïve about the necessity of maintaining a broad and resilient foundation of partnerships. A Canada that adopts the three-circle framework will be more economically secure, more geopolitically influential, and more faithful to its identity as an open trading nation grounded in ethical frameworks.

Canadian industries will gain access to new markets for growth, and Canadian foreign policy will acquire safer and more credible strategic options. For example, when faced with unreasonable demands from the United States, Canada will be able to say "no" with greater confidence, because it will no longer be dependent on a single pillar. At the same time, the United States will remain a powerful ally, but one that increasingly recognizes Canada's autonomy and independent standing.

Canada will also play a greater role in global stability: whether through infrastructure financing in ASEAN, facilitating dialogue in the Gulf region, or maintaining a more active presence in multilateral arenas beyond its traditional circle of partners. Domestically, Canadians will benefit from greater prosperity and economic resilience, with lower systemic risk, ensuring that a single tweet or foreign tariff decision can no longer abruptly endanger jobs and livelihoods.

In short, the proposed new Canadian foreign policy can transform vulnerability into strength. Rather than relying on a single axis of trade and cooperation, this approach surrounds Canada with multiple circles of partnership, functioning as a form of strategic insurance against the disruption of any single relationship. The tariff war was a harsh lesson, but if Canada learns from it, the country can emerge more resilient, more autonomous, and more durable in an increasingly fragmented world.

It is often said that every crisis contains opportunity. Canada's opportunity at this juncture lies in reclaiming agency over its economic destiny by expanding its horizons. With courage and strategic foresight, Canada can, and must, pursue this bold diversification agenda. The recommendations outlined in this report provide a roadmap, but traversing this path requires sustained political will. The time to act is now, before the next crisis arrives.

Leaders across government, academia, and industry must unite behind this agenda, and public opinion must align with the understanding that Canada's future prosperity and sovereignty depend on a more global Canada. In doing so, Canada honors the legacy of its

trade pioneers, who consistently sought new horizons, and secures its place in a rapidly changing world. As the Government of Canada stated in 2022:

"Trade diversification remains an important strategy, especially in an environment of heightened uncertainty, as it can lessen the impact of external shocks, especially in particular sectors or countries."[26]

Today, this statement is more relevant than ever. This strategy must be pursued boldly and unapologetically, so that Canada never again becomes hostage to the emotional or erratic decisions of a single partner.

[26] https://international.canada.ca/en/global-affairs/corporate/reports/chief-economist/diversification/overseas-markets-2022 (13,9,2025)

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