

**REPLACING NAFTA WITH USMCA: ASSESSING THE ECONOMIC IMPACT OF
REGIONAL TRADE EVOLUTION IN NORTH AMERICA***Bekzod Uzoqov**Master's student, Department of International Economics**University of World Economy and Diplomacy**E-mail: uzoqovbekzod2002@gmail.com*

Abstract: This study evaluates the economic impact of the United States-Mexico-Canada Agreement (USMCA) on member countries, focusing on trade volumes, foreign direct investment (FDI), and GDP growth. Using post-USMCA data and comparative analysis with the former NAFTA framework, the study reveals moderate increases in trade and FDI, particularly in Mexico. While Canada and the U.S. experienced marginal benefits, Mexico's manufacturing sector notably expanded. The findings indicate that while USMCA modernizes trade relations and enhances digital and labor provisions, its economic benefits are unevenly distributed. Recommendations suggest policy harmonization and infrastructure development to optimize integration and equitable economic growth.

Keywords: USMCA, regional trade agreements, economic impact, foreign direct investment, trade volume, GDP growth, NAFTA

Introduction

The economic landscape of North America underwent a significant transformation with the replacement of the North American Free Trade Agreement (NAFTA) by the United States-Mexico-Canada Agreement (USMCA) in July 2020. As a modernized regional trade agreement (RTA), the USMCA introduced updated provisions in areas such as digital trade, labor standards, and environmental regulations, aimed at fostering a more balanced and sustainable economic partnership among the three nations. This shift was a response to growing economic disparities and structural changes that emerged under NAFTA, prompting policymakers to revise the trade framework to better reflect contemporary global trade realities.

This article examines the economic impact of the USMCA, with a focus on changes in trade volumes, foreign direct investment (FDI), and gross domestic product (GDP) among the United States, Mexico, and Canada. By analyzing comparative data from before and after the agreement's implementation, the study evaluates whether USMCA has met its objectives of enhancing economic integration and promoting trade efficiency. While previous research has primarily critiqued NAFTA's outcomes, there is limited empirical analysis on the early effects of USMCA. This study aims to contribute to that emerging discourse by offering insights into the effectiveness of modern RTAs in promoting sustainable and equitable economic growth.

Literature review

Regional trade agreements (RTAs) have been instrumental in promoting economic integration, particularly in North America. The North American Free Trade Agreement (NAFTA), which

came into force in 1994, was a landmark in regional trade liberalization, eliminating most tariffs between the United States, Mexico, and Canada. It significantly increased regional trade, which rose from \$290 billion in 1993 to over \$1.1 trillion by 2016. NAFTA also contributed to cross-border investment, with U.S. foreign direct investment in Mexico growing from \$15 billion to more than \$100 billion during that period.

Despite these gains, NAFTA faced growing criticism. In the United States, it was blamed for job losses and stagnating wages, particularly in manufacturing. Sectors such as auto manufacturing saw sharp employment declines - about 350,000 jobs lost - while the Mexican auto sector grew substantially. Critics pointed to wage differentials and the offshoring of production to lower-cost locations like Mexico. These concerns culminated in political pressure, leading to the renegotiation of NAFTA and the formation of the United States-Mexico-Canada Agreement (USMCA), implemented in July 2020.

The USMCA retained the core structure of NAFTA but introduced key updates, including stronger labor provisions, digital trade rules, and stricter automotive rules of origin. The new rules require 75% regional content in automobiles and mandate that 40% of vehicle content come from factories paying at least \$16 per hour. These provisions aim to address wage disparities and strengthen labor rights, particularly in Mexico, which received labor-related investments in key industries such as electronics and automotive manufacturing.

The agreement also addresses digital trade by prohibiting tariffs on digital products and allowing cross-border data flows, modernizing trade rules to fit the contemporary economy. Additionally, the extension of copyright terms and protections for internet service providers created a more secure environment for digital innovation and e-commerce.

In terms of economic impact, the USMCA appears to have contributed to a surge in trade and investment in the region. By 2022, trade volume among the three countries surpassed \$1.5 trillion, and 9.5 million jobs were attributed to regional trade. Foreign direct investment increased sharply - capital investment rose by 134% to reach \$219 billion, with substantial flows from the U.S. and Canada into Mexico, particularly in manufacturing. Canada's FDI inflows from USMCA countries rose 23% between 2020 and 2022, while Mexico saw North American investment make up nearly half of total FDI in early 2023.

Nevertheless, the USMCA has also encountered challenges. Trade disputes over energy policy, labor rights, and agricultural market access have emerged, potentially affecting the stability of the agreement. Public opinion on trade has shifted, with growing protectionist sentiment in the United States. While support for trade remains strong overall, political shifts could influence future cooperation.

Overall, while USMCA has modernized the North American trade framework and stimulated investment, its long-term success will depend on political stability, effective dispute resolution, and sustained commitment to economic integration.

Methodology

This study employs a comparative quantitative analysis of key economic indicators - trade volume, foreign direct investment (FDI), and GDP growth - before and after USMCA implementation. Data is sourced from credible international organizations such as the OECD, World Bank, and UNCTAD. The research utilizes descriptive statistics and trend analysis to identify shifts attributable to USMCA. Additionally, sectoral case studies, particularly in automotive and manufacturing, provide qualitative insight. This mixed-methods approach offers a comprehensive understanding of the agreement's economic impact across the United States, Mexico, and Canada.

Findings and discussion

The USMCA, signed on November 30, 2018, and implemented on July 1, 2020, marked a vital renewal of trade relations among the United States, Mexico, and Canada. It was designed to replace NAFTA, which had been in place since January 1994, with the goal of promoting freer trade among the three countries. The agreement has successfully modernized and facilitated commerce, leading to increased employment opportunities, greater investment, and a rise in exports throughout North America. It also introduced enhanced protections for intellectual property, offering businesses greater security and encouraging investment. By streamlining trade rules and fostering fair competition, the USMCA seeks to create a balanced and prosperous trading environment for all member nations. Overall, it represents a major advancement in strengthening economic ties and supporting sustainable development within the region.

Key provisions of the USMCA:

Agriculture and Dairy: The agreement opened Canada's dairy market to U.S. farmers, allowing tariff-free access for up to 3.6% of the market value. It also aimed to expand market access for poultry products.

Intellectual Property: USMCA extended copyright terms to 70 years after the creator's death and banned tariffs on digital goods. It also established protections for internet companies through copyright safe harbor provisions.

Automotive Industry: The deal raised the required regional content for duty-free cars and trucks to 75% from the previous 62.5% under NAFTA and mandated that 40% of automotive labor must be performed by workers earning at least \$16 per hour.

Sunset Clause: Unlike NAFTA, USMCA includes an expiration clause after 16 years but allows renewal every six years through joint reviews. The agreement will only expire if the parties fail to reach consensus after ten years of annual meetings to resolve issues. The first joint review is scheduled for 2026.¹

Three years of USMCA: impact overview

As of July 2023, the USMCA has completed three years and has significantly contributed to reducing supply chain vulnerabilities, lessening reliance on China, supporting key industry development, and boosting regional industrial competitiveness, fostering creative restructuring. In response to COVID-19, the U.S. implemented policies aimed at building resilient supply chains in sectors like semiconductors, rare earth minerals, and batteries. Over this period, the agreement has facilitated job creation, increased investments, and enhanced trade within North America. Notably, trade within the region surged to USD 1.5 trillion in 2022, with free trade generating approximately 9.5 million jobs. Together, the three countries now represent one-third of the global GDP. Moreover, in the past two years, Mexico and Canada have become the United States' top trading partners, with trade volume exceeding goods trade with China by 44%.

¹ <https://www.aranca.com/knowledge-library/articles/investment-research/usmca---a-three-year-retrospective-and-its-impact>

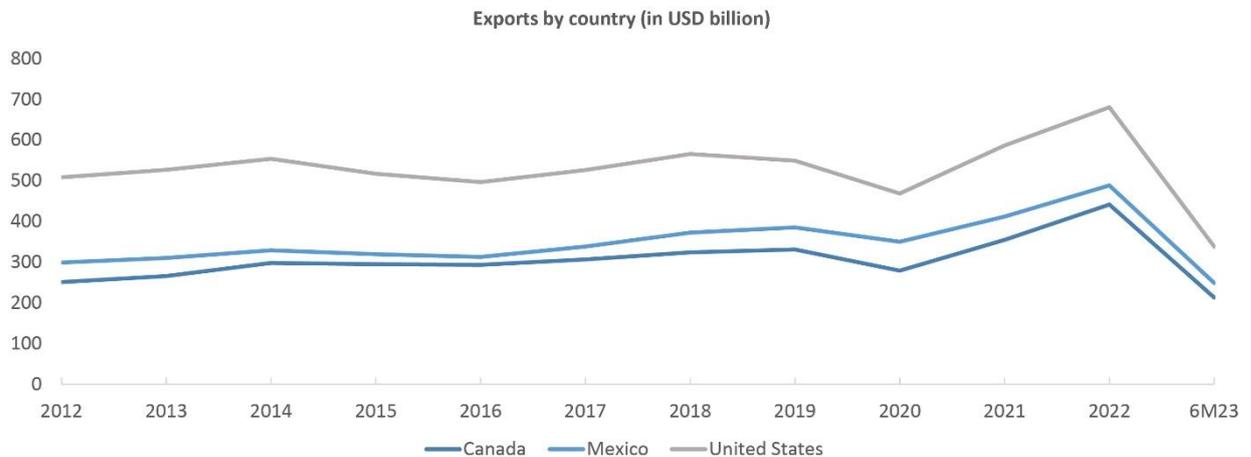


Figure 1: The value of exports by 3 countries.²

The export trends of Canada, Mexico, and the United States from 2012 to mid-2023 reveal important insights into the economic dynamics of North America. Over most of this period, exports steadily increased, reflecting growing trade integration and economic cooperation within the region. The United States consistently maintained the highest export volumes, ranging roughly between \$500 billion and \$700 billion annually, followed closely by Canada and Mexico, whose exports grew from approximately \$250 billion to over \$400 billion. However, the global COVID-19 pandemic in 2020 caused a sharp decline in exports across all three countries, as supply chains were disrupted and demand fell worldwide. This downturn was followed by a strong rebound in 2021 and 2022, with total trade peaking near \$1.5 trillion in 2022 - a recovery likely supported by the early implementation of the USMCA agreement, which helped stabilize and enhance trade flows. The surge in exports during this recovery phase demonstrates the resilience of the North American economies and their ability to adapt to global shocks. Yet, early 2023 saw a notable slowdown in exports, with values dropping sharply, underscoring the continued vulnerability of international trade to external pressures such as inflation, geopolitical tensions, and fluctuating global demand. Overall, this export data highlights both the deep economic interconnection of the USMCA countries and the ongoing challenges they face in maintaining steady growth amid a complex global environment.

Increased investments (FDI and intra-regional investments). The USMCA has significantly boosted investment activity within the North American region. Capital investments surged by an impressive 134% following the agreement's implementation, reaching a total of USD 219 billion. The United States emerged as a major recipient of these investments, with over 11% of foreign direct investment (FDI) originating from Mexico and Canada. In the first quarter of 2023, Mexico attracted USD 29.04 billion in inward FDI, nearly 46% of which came from North American partners. Notably, the share of FDI directed toward Mexico's manufacturing sector more than doubled, rising from 24% to 56.9%. During this period, approximately half of the new investments in Mexico originated from Canada and the U.S. Similarly, nearly 50% of Canada's FDI in 2022 was sourced from other USMCA member countries. Between July 2020 and March 2023, the U.S. invested nearly USD 31 billion in Canada and USD 28 billion in

² Banco de Mexico, Statistics Canada (2023), US Census Bureau

Mexico, while Canada invested USD 17.7 billion in the U.S. and USD 2.8 billion in Mexico. Mexico's investments amounted to USD 2.8 billion in the U.S. and USD 0.1 billion in Canada. **Supply chain resilience.** USMCA has also played a crucial role in strengthening supply chain resilience by encouraging increased investments in strategic industries across North America. There has been notable growth in sectors such as electric vehicles (EVs), semiconductors, emerging technologies, and infrastructure development, which together enhance the region's capacity to withstand future disruptions. Over the next decade, key legislative initiatives including the Bipartisan Infrastructure Bill, the CHIPS and Science Act, and the Inflation Reduction Act (IRA) are projected to attract investments totaling approximately USD 3.5 trillion. Canada has complemented these efforts by establishing a USD 1.5 billion Critical Minerals Infrastructure Fund and allocating nearly USD 4 billion toward its 2022 Critical Minerals Strategy. Additionally, the 2020 Canada–U.S. Joint Action Plan on Critical Minerals aims to bolster bilateral mineral trade valued at over USD 95.6 billion, further solidifying regional supply chain integration.

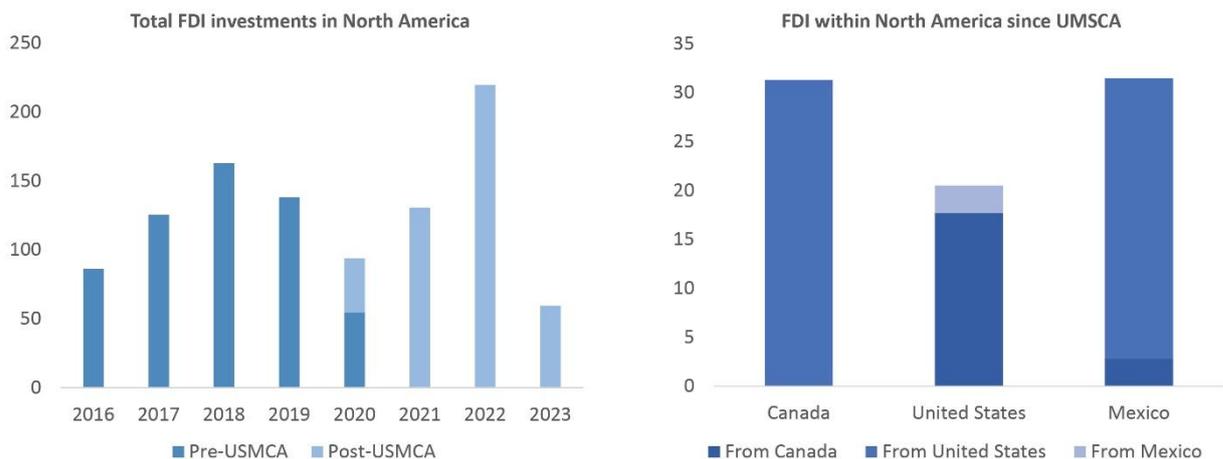


Figure 2: FDI dynamics in North America: before and after USMCA

The charts show that foreign investment in North America grew significantly after USMCA was implemented, especially peaking in 2022. This suggests the agreement helped create a better environment for investors. The breakdown of investment flows reveals strong financial ties between the US, Canada, and Mexico, with each country investing heavily in the others. This means USMCA not only increased overall investments but also strengthened economic connections within the region. It highlights how trade agreements can boost confidence and cooperation among neighboring countries.

Conclusion

The transition from NAFTA to USMCA has marked a significant modernization of North American trade relations. While preserving the foundational framework of NAFTA, the USMCA introduced critical updates that reflect the evolving global economy - particularly in labor standards, digital trade, and environmental protections. Empirical data from the first three years post-implementation indicate that the agreement has generated substantial gains in regional trade volumes and FDI, especially benefiting Mexico's manufacturing sector. However, the uneven distribution of economic benefits and persistent trade disputes highlight the need for



continued policy coordination and commitment to equitable integration. Moving forward, ensuring political stability, enhancing infrastructure, and leveraging strategic industrial policies will be essential to maximizing the long-term benefits of the USMCA for all member nations.

References:

1. Office of the United States Trade Representative (USTR). (2023). USMCA Fact Sheet. Retrieved from <https://ustr.gov/>
2. OECD. (2023). International Trade and Balance of Payments Statistics. <https://www.oecd.org>
3. UNCTAD. (2023). World Investment Report 2023: Investing in Sustainable Energy for All. <https://unctad.org>
4. World Bank. (2023). World Development Indicators. <https://data.worldbank.org>
5. Global Affairs Canada. (2023). Canada's State of Trade Report 2023. <https://www.international.gc.ca>
6. Secretaría de Economía (Mexico). (2023). Foreign Investment Statistics. <https://www.gob.mx/se/>