Tariff Policy
Bankruptcy Industry Update

Restructuring Professionals in Canada and Mexico Prepare for Increased US Protectionism

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As financial markets gird for a more protectionist U.S. trade policy, restructuring professionals north and south of the United States are preparing for an increase in creditor negotiations, particularly in the integrated automotive sector.

Although Canada and Mexico skirted broad national tariffs on goods for a month, they are now subject to a new 25% import tariff into the United States on steel and aluminium. The two countries, which are among the largest exporters of steel products to the U.S., should prepare for a U.S. economic policy that makes additional tariffs on other exports likely, experts said.

"Tariffs are probably coming on Canada and Mexico and other trading partners," said Rachel Ziemba, senior fellow at the Center for a New American Security. "The question is whether they will come related to this migration and drugs trigger, or as part of USMCA renegotiations next year or in another context."

Furthermore, the impact of tariffs would likely spread beyond autos and may bring about company and creditor discussions or restructurings in other sectors such as industrials, agriculture, and food and beverage, according to experts.

Mexico and Canada are both highly dependent on trade with the United States, with goods sent from Mexico to its northern neighbor representing 83% of total exports in the first 11 months of 2024, according to Mexico's national statistics agency, while 77% of Canadian exports were sent to the United States, according to Statistics Canada.

Additionally, tariffs could stifle each economy. A report by Fitch Ratings found that the introduction of a 25% tariff could lead to a recession in Mexico and reduce the country's output by 3% by 2026. Canada's central bank benchmarked national GDP to be 2.5% lower in the first year of sustained tariffs between the two countries than it would have otherwise been.

Autos in Focus

Sharp focus has been drawn to the automotive sector, where parts for automobiles can cross international borders several times before original equipment manufacturers, or OEMs, produce the final product.

The automotive industries in Mexico and Canada are the seventh and 13th largest in the world, respectively, and are closely tied to U.S. supply chains, with 76% of vehicles produced in Mexico and 88% of vehicles produced in Canada being exported to the United States in 2023. Even if the broad tariffs are not imposed, analysts expect that the automotive industry will be the target of increased protectionist measures in coming years.

North American automotive companies have been adapting to increased trade barriers in the form of expanded rules of origin, or ROOs, introduced in the USMCA, which set minimum percentages of inputs that must originate in USMCA countries for a vehicle or auto part to be exempted from tariffs. The ROOs began to be phased in after the USMCA's signing in 2020 and are expected to fully come into effect for all exporters in 2025 and 2026.

Reports by the U.S. International Trade Commission and the U.S. trade representative have found that the ROOs have already led to reduced imports of light vehicles from Canada and Mexico and increased imports from the rest of the world, as well as an increase in vehicles and part imports that are subject to tariffs.

Many in the auto industry are concerned that the ROOs could be made even stricter when the USMCA is renegotiated in 2026. Such increased protectionist policies by the United States, as well as increased compliance audits by the Mexican government of the IMMEX import duty deferral program, could increase pressure on the Mexican automotive industry in coming years, according to sources.

Since most OEMs operating in Mexico are large foreign companies, they will likely be able to absorb the coming disruptions. But some players in the auto parts sector, which includes some Mexican companies, may be more vulnerable, sources said. Spreads on some bonds issued by Mexican auto parts producers, including Nemak and Metalsa, have widened since Trump's victory in November 2024 before contracting somewhat after the tariff deferral was announced.

Larger OEMs, while not threatened by insolvency, have flashed concern over the impact of tariffs to the auto sector broadly. Ford Motor said on its fourth-quarter 2024 earnings call that tariffs longer than a few weeks "would have a huge impact on [the] industry with billions of dollars of industry profits wiped out [and an] adverse effect on U.S. jobs, as well as the entire value system in [the] industry."

Large OEMs with Canadian exposure should similarly be able to pass on costs or squeeze suppliers, sources mentioned. Yet auto component suppliers, especially those in the electrical vehicle supply chain, are already cash-strapped owing to delays with electric vehicle launches, according to a PwC presentation.

Distressed auto parts companies have many options to address tariffs. From a restructuring vantage point, if there is an ability to repatriate production lines as a part of a restructuring, that could accelerate, according to one source. There have been a number of restructuring in the past few years where production has returned stateside, such as Accuride, albeit not yet as a byproduct of tariffs, sources noted.

Distress Elsewhere

North American companies outside of the autos and auto parts sector should also carefully examine their exposure to cross-border supply disruptions.

In addition to the automotive sector, Canadian industries affected by tariffs are "potentially widespread," according to President Bobby Kofman and Vice President Noah Goldstein at KSV Advisory, a Canadian restructuring advisory firm. "It's every industry, it's food, it's lumber, it's oil and gas, railways," they added.

Other sources pointed to the lumber and diary industries in Canada as potential flashpoints for the U.S. government given past disagreements over Canadian policy. The U.S. lumber industry in particular, as one source noted, has been very vocal about Canadian policy toward lumber, although large lumber companies should be able to take on additional cost, they added.

The imposition of broad tariffs could also cause ripple effects throughout the Mexican economy, in addition to affecting companies in certain sectors that are dependent on exports, said Iván Romo, managing partner of SOELI Consulting.

An Octus, formerly Reorg, analysis of private company transcripts found that industrial companies brought up tariffs more often than any other sector on recent earnings calls, followed by consumer discretionary and materials. A survey of over 300 Canadian manufacturing companies echoes this finding, with about half of the respondents saying they would consider postponing capital investments and shifting production to the United States if tariffs are implemented. The survey, by trade group Canadian Manufacturers & Exporters, also found that about a third of respondents have already postponed planned investments as tariffs become front of mind for North American business leaders.

“I think that the number of businesses that end up in insolvency or restructuring could increase, because the tariffs could have a big impact on economic conditions,” Romo said. “I think the effect would be generalized, more than on any specific business, and it could contribute to a wave of restructurings.”

The Role of Restructuring

Though broad tariffs against Canada and Mexico have yet to be implemented, restructuring professionals foresee companies preparing a war chest to handle situations triggered by weighty tariffs.

Joseph Pasquariello, partner and a head of the restructuring group at Goodmans LLP, said he expects companies to view trade sabre rattling as a “not so early warning sign” and to engage in discussions with their creditors. “I do think [discussions are] going to be something we’re going to see more of, that type of early interaction on some covenant holidays … or some amendments in the near term if these tariffs take hold.”

The specter of tariffs may also complicate restructuring matters, according to Kofman and Goldstein. “If these tariffs are long-lasting, it could have long-term secular implications where capital providers do not want to participate and buyers disappear.” Additionally, distressed businesses may have more trouble finding the rescue capital needed in a restructuring, they added.

In the event that companies do seek court protection, Pasquariello noted that the Companies’ Creditors Arrangement Act, the Canadian federal restructuring act, is generally “not as codified or hardwired as chapter 11 from both a substantive and process/timing perspective,” granting companies and their creditors the speed and creativity needed to effectuate a restructuring. “We can usually accomplish things in a quicker time frame than what companies can achieve in a chapter 11,” a trait he thinks would be crucial in restructurings related to the tariff shock.

Whether or not further tariffs are levied within North America, analysts and experts point to a shift in how Canadian and Mexican businesses should view the U.S. market. While the automotive sector is front and center as governments negotiate a new trade relationship, the companies potentially affected span many industries.

The magnitude of restructurings tied to tariffs is too early to tell, but professionals agree that long-lasting tariffs would make an already busy time even busier.
