THE WALL STREET JOURNAL.

Steel and Aluminum Tariffs Could Leave Canada's Housing Sector on Shakier Foundation

Rapidly rising costs for construction steel come as housing market is cooling

The escalating trade quarrel between Canada and the U.S. is ringing alarms in Canada's housing sector. Photo: James MacDonald/Bloomberg News

By Vipal Monga and Kim Mackrael
June 6, 2018 4:59 p.m. ET

TORONTO—An escalating trade quarrel between Canada and the U.S. over steel and aluminum tariffs is ringing alarms in Canada's housing sector, as surging costs for construction steel add pressure to a cooling residential real-estate market.

The cost of construction steel, used to build condominiums, has already jumped as much as 50% during the past year to 1,400 Canadian dollars a ton, thanks to the expected tariffs and a strong construction market, said **Richard Lyall, president of the Residential Construction Council of Ontario**, a provincial trade group.

After the U.S. last week placed tariffs on steel and aluminum imports from Canada and other allies, Canadian Prime Minister Justin Trudeau announced matching tariffs on U.S. imports: 25% on steel and 10% on aluminum.

The retaliatory tariffs, which are set to begin July 1, could push the cost of construction steel to as much as C$2,000 a ton, Mr. Lyall said. That means developers in Toronto building a 30-story condominium tower that uses 2,000 tons of steel would face C$2 million in extra costs.

“This could be the steel that breaks the camel’s back,” said Mr. Lyall, whose group is calling for moderation in Canada’s plan.

In recent years, major cities including Toronto have seen a building frenzy. Photo: Brent Lewin/Bloomberg News

Major Canadian cities including Toronto and Vancouver have experienced a building frenzy in recent years, with construction cranes and new high-rises dotting the horizon and house prices rising. Now, developers are struggling with higher land prices and increased regulations, said Benjamin Tal, deputy chief economist for CIBC World Markets Inc.

“Construction costs have already been rising very rapidly, and the steel aspect of this is very major,” he said. “It will take margins that were already shrinking and make them lower.”

Central bank officials previously identified imbalances in Canada’s housing sector as a vulnerability in the country’s overall economy, in part because of speculative behavior by real-estate investors in Toronto and Vancouver. Deputy governor Sylvain Leduc said recently the bank expects rising wages and high consumer confidence to continue to support housing construction and consumption growth.

However, the pace of home building slowed in April, with housing starts falling almost 5%, and some economists anticipate a further cooling, as developers deal with higher construction costs and as overall housing activity slows. Canadian building permits, which can give an early indication of building activity, fell 4.6% in April, according to data released Wednesday.

“To the extent that now these tariffs on steel will also put upward pressure on prices, that will also have a cooling effect,” said Chris Gardner, president of the Independent Contractors and Businesses Association in British Columbia. Condominium developers who presold units could be particularly squeezed in the short term, he said.

Tougher mortgage-financing rules, introduced in January, have also hit real-estate markets in many Canadian cities. Sales of existing homes fell nearly 3% in April from a year earlier, while prices rose at the slowest pace in nearly nine years, according to the Canadian Real Estate Association.

The slowdown weighed on economic growth during the first quarter, with Canada’s gross domestic product rising 1.3% from a year earlier—falling short of market expectations for a 1.9% increase.

Mr. Gardner said that while lack of supply is a bigger concern, there’s a risk the new tariffs could push housing markets into a steeper correction. “Overall, I think we’re in a situation where the timing of these tariffs could not have been worse,” he said.

Alan Vihant, executive vice president at Great Gulf, one of Canada’s largest developers, says he has seen costs of construction steel for his projects rise between 10% and 15% this year, partially because real-estate markets in Canada and the U.S. are strong. Tariffs may only add to the cost inflation, he said.

The costs hurt developers who are already struggling with higher taxes and levies from local governments, Mr. Vihant said. “We’re getting squeezed on margins from all over.”