Steel Yourself

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The U.S. Administration announced this week that Canada's exemption from tariffs on steel and aluminum will indeed expire June 1st, imposing duties of 25% and 10%, respectively, on shipments of these products. We believe **the direct economic impact in Canada will likely be moderate at around 0.1% of GDP**, in part because much of the move will be absorbed through the price channel, especially for aluminum. Even so, this is clearly a negative development with respect to future trade talks and potential disruptions in other sectors, such as autos.

Canadian and U.S. trade in raw and processed steel is well balanced. According to StatsCan's latest data, Canada exported a total of $13.3 billion of these goods to the U.S. in the latest 12 months, up 17% from the prior year and accounting for 3% of total exports to the States. More than $900 million of that total represents re-exports from other countries, which have jumped in recent months. Meantime, Canada imported $12 billion of raw steel and products from the U.S. over that period, up 10% from the prior year. The moderate trade surplus follows a consistent string of bilateral deficits in steel goods from 2009 to 2015 (inclusive). Stretching back to the start of the FTA in 1989, Canada has tended to run a small surplus in steel trade—with the ratio of exports to imports averaging about 1.06 to 1.00 (last year it was 1.07 to 1.00), or nearly balanced.

True, it is a different story for aluminum, where Canada is by far the main supplier for the U.S. market. Canadian sales of aluminum and articles to the U.S. totaled $11 billion over the latest 12 months, compared with $3.6 billion of imports. But that is a classic case of comparative advantage (i.e. low electricity prices in Quebec).

The Administration's proposed tariffs are designed to support U.S. steel and aluminum makers, but they don't seem to need much help. Prices of these metals have been on an upswing, even if aluminum has faded in the past month, while combined shipments were up 12% y/y in Q1. New orders of aluminum are up similarly, while steel bookings have jumped 15%. The strength in these two industries suggests the tariff will be largely passed on to users in the form of higher prices. In other words, consumers will be the biggest losers, as is always the case with protectionist measures.

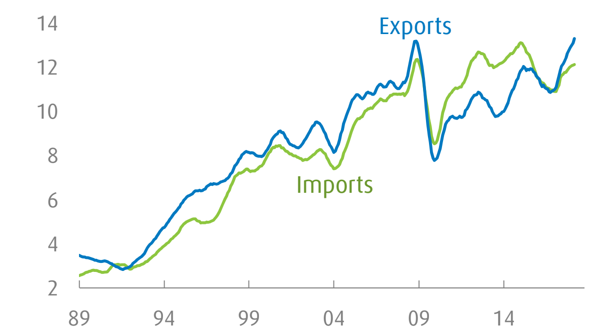
Regionally, Ontario and Quebec are most exposed to steel and aluminum, with exports from the latter weighing in at nearly 2.5% of GDP. That said, the bulk of Quebec's exports are in aluminum, so if producers in that sector are able to pass on much of the tariff through higher prices, the economic impact would be relatively modest. Atlantic Canada carries little direct exposure, while exports from B.C. and the Prairies all weigh in at less than 0.5% of GDP.

Bottom Line: The bigger concern is the threat of broader trade actions, whether the retaliatory measures from Canada and/or further moves from the U.S., particularly if this serves as a template for the auto industry.

Chart 1
Relatively Balanced

Canada (C$ blns : n.s.a.)

Iron and Steel Trade with U.S.[1]

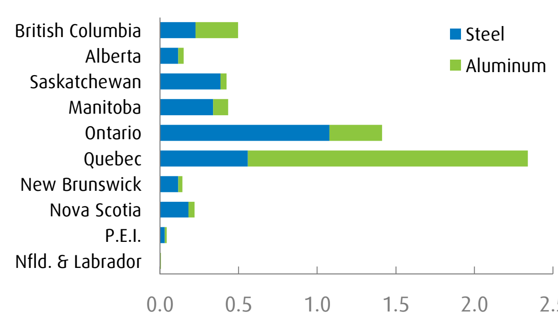


[1] including products
Sources: BMO Economics, Haver Analytics

Chart 2
Regional Impact

2017 (% of provincial GDP)

Steel and Aluminum Exports to U.S.[1]



[1] raw and processed
Sources: BMO Economics, Haver Analytics