HIGHLIGHTS

• The total consumer price index (CPI) rose only 0.1% in January, taking the total annual inflation rate from 0.8% to 0.5%.
• The core index (CPIX), which excludes volatile components, also rose 0.1% that month. Its annual change fell to 1.0% from 1.1% in December.
• Retail sales dropped 2.1% in December, performance that is far below expectations.
• In real terms, retail sales fell 1.6%.

COMMENTS

The results released this morning by Statistics Canada are worrisome at first glance. The total annual inflation rate continued to fall. At only 0.5%, some could now fear that inflation will drop closer to zero in the coming months, and that the country may even be on the verge of deflation. However, everything suggests that total inflation has reached its cyclical low and that February could bring some stabilization or even an increase. For one thing, seasonal effects usually result in a 0.3% rise by total CPI in February. For another, weekly surveys of prices at the pump show an average increase of 7.4% in gas prices for the first three weeks of February. This component alone should produce a 0.4% rise in the CPI. All in all, total CPI monthly growth could easily be around 0.7% in February, a situation that would put the total annual inflation rate at 0.8%.

For retail trade, the automotive sector certainly steepened December’s drop by sales, but the 0.9% decrease by other activity sectors points to more widespread problems. This weak result really stands out from the more encouraging data that has been posted by retail trade since last summer.

However, several favourable factors remain in place. The labour market is performing rather well, incomes are up and consumer confidence improved substantially in January. Under these circumstances, a rebound by retail sales could be seen as of January. It is also possible that the expanding gift card phenomenon could once more affect retail sales results for December. Note that sales are not recorded until the card is exchanged for goods at a retailer, thus reducing sales for December and inflating those for January.

Implications: The coming stabilization by inflation should reassure Canada’s monetary authorities. Key rates should therefore remain where they are for several more quarters. As for the drop by retail sales, it introduces a downward risk for the monthly change in real GDP by industry. However, expectations for economic growth in December, as well as for the fourth quarter as a whole, were already quite low.

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