Canada: A Temporary Drop in Inflation

HIGHLIGHTS

- The total consumer price index (CPI) fell 0.4% in December, in line with our expectations.
- The main components that contributed to this decrease are telephone services (-7.6%), gas (-3.3%), tour packages (-6.6%), traveller accommodation (-6.9%) and men’s clothing (-5.0%).
- In contrast, the components that contributed to the rise are motor vehicle purchases (+0.9%), fresh vegetables (+4.8%), air transport (+3.5%), fresh fruit (+2.3%) and mortgage interest costs (+0.5%).
- The annual change in total CPI went from 2.1% in November to 1.9% in December.
- Overall for 2017, the total annual inflation rate was 1.6%, compared with 1.4% in 2016.

COMMENTS

As expected, arithmetic effects led to a drop in the annual change in the total CPI in December. This phenomenon should even intensify in January as the annual change could fall closer to the lower target. That being said, a relatively quick return to the mid-point target (2%) can be expected to follow as fundamental trends reassert themselves. Among other things, some inflationary pressures should be increasingly felt as excess production capacity is absorbed.

IMPLICATIONS

Despite some blips, inflationary pressures recently appear to be higher, which contrasts with the persistent weakness in total inflation observed in recent years. Two of the Bank of Canada’s three benchmark indexes were up in December. On average, the annual change was 1.8%, which is very close to the mid-point target. This obviously opens the door to further key interest rate hikes in the coming months.

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