Canada: Lower Inflation than Expected and Disappointing Retail Sales

HIGHLIGHTS

- The total consumer price index (CPI) rose only 0.1% in May, well below expectations.
- The total annual inflation rate stays at 2.2%.
- The average annual change of the three benchmark indexes is 1.9%, down slightly from last month’s 2.0%.
- Retail sales fell 1.2% in April. Most forecasters expected no noticeable change in the month.
- In real terms, sales saw a monthly decline of 1.4%.

COMMENTS

There are many reasons why monthly growth of the total CPI was weaker than anticipated. First, gas price hikes were lower than expected. Second, there were practically no seasonally adjusted price increases, whereas they are usually around +0.2% in May. Third, the CPI trend was still quite weak, while the seasonally adjusted version was up only 0.1%. That said, the trend should speed up in the coming months as excess capacity becomes absorbed.

April’s decline in retail sales is due to a sharper than expected drop in automobile sales. The rainy weather must have delayed some sales, as evidenced by the 3.3% reduction in sales of construction materials, and gardening materials and supplies.

IMPLICATIONS

While we thought total inflation would get closer to the higher target (3%) in the coming months, weaker May results hint that the annual change in total CPI will remain near the median target (2%). That gives the Bank of Canada (BoC) more flexibility in managing its monetary policy.

Unless we get more bad news in the next few days, the inflation results should not prevent the monetary authorities from raising the overnight rate in July, as expected. But the BoC may still wait several more months before hiking key rates after that.

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Graph

Total annual inflation will rise less than initially anticipated

Sources: Statistics Canada and Desjardins, Economic Studies