

ECONOMIC NEWS

Canada: Highest Inflation since March 2003

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HIGHLIGHTS

- ▶ The consumer price index (CPI) was up 0.2% in August.
- ▶ The key components fuelling this increase were air transportation (+37.5%), traveller accommodation (+12.0%), other owned accommodation expenses (+1.1%), homeowners' replacement cost (+0.7%) and passenger vehicles purchases (+0.5%).
- ▶ In contrast, the components detracting from growth were tour packages (-23.7%), fresh vegetables (-2.2%), telephone services (-1.7%), mortgage interest costs (-0.6%), and sports and exercise equipment (-3.3%).
- ▶ The total annual inflation rate climbed from 3.7% to 4.1%, marking the highest inflation rate in about 18 years.
- ▶ The annual average variation in the Bank of Canada's (BoC) three benchmark indexes rose to 2.6% from 2.4% the previous month.

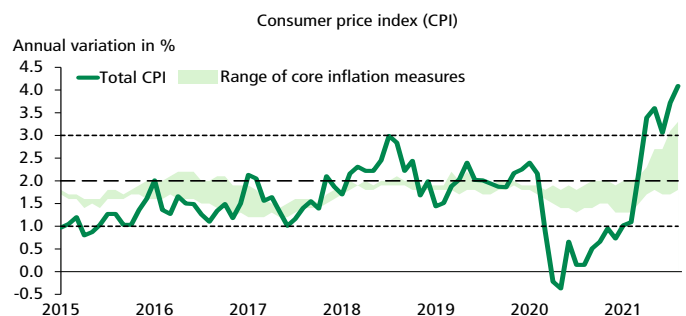
COMMENTS

As expected, the total annual inflation rate continued its upward trend in August. Naturally, there are temporary factors that continue to drive inflation, such as gasoline. However, the acceleration in price growth is becoming increasingly widespread. Based on our estimates, 54.2% of total CPI basket components saw annual price growth above the BoC's upper target (3%) in August. Clearly, many goods and services are being affected by demand and supply imbalances.

IMPLICATIONS

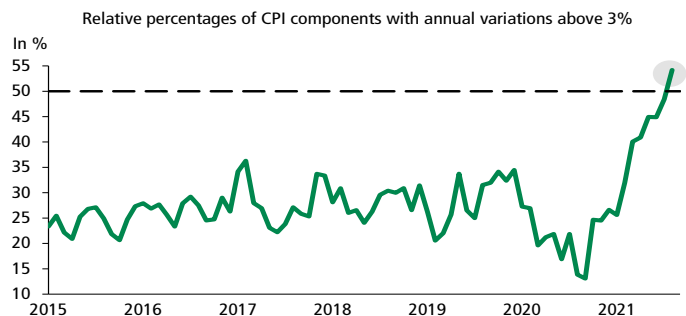
Our projection is that the annual inflation rate could peak within a few months, then gradually pull back, as the upward pressure from certain temporary factors subsides. However, the risks tied to this forecast are markedly upside. With such inflation levels, the BoC is increasingly hard-pressed to justify the extent

GRAPH 1
Total inflation rises above 4%



Sources: Statistics Canada, Bank of Canada and Desjardins, Economic Studies

GRAPH 2
More than half of CPI basket components saw inflation above 3%



CPI: Consumer price index
Sources: Statistics Canada and Desjardins, Economic Studies

of current monetary stimulus. As a result, a further tapering of bond purchases could be announced at its next meeting in October.