



Inflation uptick, economic slowdown poses challenge for Bank of Canada

We saw unwelcome news on the inflation front today as headline growth re-accelerated in August to a 4.0 per cent year-over-year pace to stray further away from the Bank of Canada's two per cent target. This was up from 3.3 per cent and marked the strongest increase since April. Prices were up 0.4 per cent month-to-month, which decelerated from July but jumped up on a seasonally- adjusted basis by 0.6 per cent. Today's inflation print suggests interest rates may need to move higher, but we expect the soft economy and cumulative impacts of past rate hikes to remain keep the Bank on hold for the remainder of this year.

The latest acceleration in inflation partly reflects the now common story of gasoline price volatility. Prices peaked in mid-2022 and subsequent declines, including a 9.6 per cent drop in August 2022 due to higher global production, contributed to base-period driven increases. Gasoline prices were up 0.8 per cent year-over-year in August after a 13 per cent decline in July. Food prices did not contribute to the increase but remained elevated at 6.8 per cent, down from 7.8 per cent, year-over-year in July. Deceleration in food prices reflected slowing growth at the grocery aisle (from 8.5 per cent to 6.9 per cent), as price growth eased for meat, dairy, and baked goods, among others.

Nevertheless, prices broadly increased with the consumer price index excluding food and energy up 3.6 per cent from 2.8 per cent. Shelter costs (up 6.0 per cent from 5.1 per cent) accelerated with the recent interest rate hikes feeding again into the shelter index. Bank of Canada inflicted increases to mortgage interest costs nudged up to 30.9 per cent year-over-year from 30.5 per cent which offset lower replacement costs, while rent rose to 6.5 per cent from 5.5 per cent. The latter is in part owed to the high interest rate environment which has pushed more households into a tight rental market. Excluding mortgage interest costs, prices moved up from 2.4 per cent to 3.2 per cent.

Among other goods, vehicle price growth was unchanged at about 2.2 per cent, furniture is 3.2 per cent lower, and household appliances are down from a year ago. Clothing and footwear costs were up mildly from a year ago by 1.7 per cent but have accelerated.

While there are plenty of moving parts in the inflation numbers the numbers were not constructive. Bank of Canada core inflation measures accelerated during the month with the trim (3.9 per cent) and median (4.1 per cent) accelerating, while the common measure held steady at 4.8 per cent. All measures remain much too high relative to the target. Monthly trim and median measures accelerated to 0.44 per cent from 0.34 per cent. Meanwhile, the 3-month all-items trend accelerated to a 6 per cent annualized pace, and 3.6 per cent excluding food and energy.

This latest CPI (Consumer Price Index) print puts the Bank of Canada in a challenging position. Inflation is not coming down as quickly as hoped, and more volatility is ahead. Base year effects from gasoline price will ease in coming months, but re-emerge late in the year, while prices have recently trended higher. At the same time, it seems clear the economy has rapidly cooled down. GDP growth was revised lower for the first half, including a slight contraction in Q2 which has curbed talk of excess demand. This is likely to keep the Bank of Canada on the sidelines for the remainder of the year, but inflation patterns could push out talks of rate cuts.

Canada Consumer Price Index

Period	2023M06	2023M07	2023M08
<i>All-Items</i>			
Actual y/y %ch.	2.8	3.3	4.0
Actual, m/m %	0.1	0.6	0.4
Seas. adj., m/m %	0.3	0.6	0.6
<i>CPI by Select Product Group, y/y % ch.</i>			
Exc. food and energy	3.5	3.4	3.6
Goods	1.4	2.3	3.7
Services	4.2	4.3	4.3
Food	8.3	7.8	6.8
Shelter	4.8	5.1	6.0
Gasoline	-21.6	-12.9	0.8
<i>Bank of Canada Core Measures, y/y % ch</i>			
Common	5.1	4.8	4.8
Trim	3.7	3.6	3.9
Median	3.9	3.9	4.1
<i>3-mth trend, seasonally-adjusted (ann.)</i>			
All-Items	3.1	3.4	6.0
Exc. food and energy	2.5	2.8	3.6

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