Economic Commentary

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central 1 Economics

Inflation takes a big step back in January

Canadian CPI inflation recorded a surprisingly sharp decline in January which should provide some impetus for a Bank of Canada rate cut in coming months. Headline CPI came in at 2.9 per cent year-over-year, down from 3.4 per cent in December, and well below consensus for a 3.3 per cent reading. This was the first time since June that 12-month growth fell below three per cent and into the target range and compared to a U.S. reading of 3.1 per cent. On a month-to-month basis, the CPI index was flat and once adjusted for seasonal factors, down 0.1 per cent.

January patterns were positive. Gasoline was the main drag on headline growth with a 4.0 per cent year-over-year decline after December's base-year driven uptick. Gas prices have moved lower with underlying oil prices. Food price inflation slowed sharply to 3.9 per cent y/y, compared to 5.0 per cent in December with seasonally-adjusted growth slowing to 0.1 per cent m/m. Broadly, price growth slowed with meat (2.8 per cent), fruit (1.9 per cent), and vegetable prices (1.6 per cent) at well behaved levels. Restaurant food prices remained stronger at 5.1 per cent. Excluding food and energy, year-over-year growth came in at a manageable 3.1 per cent.

Housing-related pressure remained a hefty driver of inflation with shelter accelerating to a 6.2 per cent year-over-year increase from 6.0 per cent in December with month-to-month growth at 0.3 per cent (s.a). Mortgage interest costs rose 27.4 per cent y/y, which ticked down from December, while rent accelerated to 7.9 per cent. This more than offset any moderation in replacement costs (-1.6 per cent).

Among other components, cellular services were down 9.1 per cent but was an upward contributor to inflation given a 14.6 per cent drop in December. Meanwhile, childcare prices were down 14.4 per cent. Household appliance prices fell 2.1 per cent with furniture down 0.8 per cent from a year ago. Vehicle prices were well behaved at 2.2 per cent. Air travel costs plummeted 14.3 per cent, albeit travel accommodation fell 1.2 per cent.

Overall, January's CPI report was indicative of a broad easing inflation pressure. Goods pricing was only 1.3 per cent higher from a year ago, and services, up 4.2 per cent, were driven by shelter. The Bank of Canada's core measure all declined including a half point drop in the core-common measure to 3.4 per cent, while three-month annualized growth in the trim- and median- measures came in at 3.2 and 3.3 per cent.

While core inflation is still above target, the Bank of Canada should be looking towards rate cuts at this point given the outsized influence of shelter costs. CPI excluding shelter came in at a tepid 1.5 per cent and the index excluding mortgage interest at 2 per cent. Elevated shelter inflation reflects high policy rates and factors outside the Bank's ability to contain. In the latter, growth is currently being driven by high demand from immigration and insufficient supply, which is outside the influence of monetary policy, while interest rates are also an impediment to new development. As much as we think it is appropriate, an April cut is likely off the table at this point given recent labour market, wage, and GDP data, but the soft January CPI reading supports a cut at the June 5 meeting.

Canada Consumer Price Index			
Period	2023M11	2023M12	2024M01
All-Items			
Actual y/y %ch.	3.1	3.4	2.9
Actual, m/m %	0.1	-0.3	0.0
Seas. adj., m/m %	0.3	0.3	-0.1
CPI by Select Product Group, y/y % ch.			
Exc. food and energy	3.5	3.4	3.1
Goods	1.4	2.4	1.3
Services	4.6	4.3	4.2
Food	5.0	5.0	3.9
Shelter	5.9	6.0	6.2
Gasoline	-7.7	1.4	-4.0
Bank of Canada Core Measures, y/y % ch			
Common	3.9	3.9	3.4
Trim	3.5	3.7	3.4
Median	3.5	3.5	3.3
3-mth trend, seasonally-adjusted (ann.)			
All-Items	1.8	2.3	1.8
Exc. food and energy	3.3	3.6	2.4

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