



Inflation beats a surprise retreat in February, rate cuts in sight

Today's soft inflation report is a sufficient signal for the Bank of Canada that a cut to the policy rate should come sooner rather than later as the stalling economy eases price pressures. Highlighting some of the folly of forecasting monthly movements in economic data, February CPI inflation fell to 2.8 per cent y/y from 2.9 per cent in January, which was far below the consensus for an increase to 3.1 per cent. On an unadjusted basis, prices rose 0.3 per cent m/m or half of consensus, with a seasonally adjusted gain of 0.1 per cent. This compared to a U.S. acceleration to 3.2 per cent from 3.1 per cent.

It was a good news story all around in February with the first back-to-back reading below three per cent since March 2021. Despite a lift from gasoline prices, which rose four per cent m/m, and saw its y/y decline flip from a 4.0 per cent decline to an increase of 0.8 per cent, other drivers eased more than offset. Food prices were unchanged m/m with a 3.3 per cent y/y gain which was the lowest since August 2021. Cost pressures continued to ease across food products with meat up 2.8 per cent, dairy 0.8 per cent, a drop in fruit prices, and slowing in baked goods. Restaurant price growth remained elevated at 5.2 per cent y/y. Excluding volatile food and energy, the overall index was a touch lower than the headline, pointing to a broader slowdown. Statistics Canada highlighted declining cellular plans (-26 per cent) costs as a driver of lower inflation, although clothing prices also declined sharply (4.4 per cent), while furniture (0.6 per cent) and appliances (-2.2 per cent) saw negative or little growth.

Shelter remained a counterweight to these easing price patterns with shelter accelerating to 6.5 per cent from 6.2 per cent on a 0.4 per cent m/m increase. Rent rose to an 8.2 per cent y/y increase, which was the highest since the early 1980s. Owned accommodation was steady at 6.7 per cent y/y amidst some easing in mortgage interest component (up 26.6 per cent) and easing replacement costs (-1.4 per cent). Shelter continues to feed into core measures of inflation but as we have noted, several factors are driving these costs. Higher interest rates have contributed to higher mortgage interest costs, while massive population growth continues to put upward pressure on rental accommodations. Excluding shelter costs, overall inflation is a down to 1.3 per cent, and 1.9 per cent if we only exclude mortgage interest.

For the Bank of Canada, there remained much to ponder as it looks to timing of a rate cut but we think it should be soon. Core inflation remained constructive. The Bank's three measures of core inflation declined by 0.2 percentage point with the common- and median measures down to 3.1 per cent and the trim- at 3.2 per cent. Moreover, the trend is clearly in the right direction. The three-month annualized change in headline and exc. food/energy is below 1.5 per cent, with core trends sitting at 2-2.5 per cent. Shelter remains a challenge, but lower interest rates will further ease inflation and population driven demand (alongside supply constraints) are outside the Bank's control, meaning it will need to look through this driver. While U.S. CPI trends are source of caution, we expect inflation to further ease as the economic slowdown continues and robust growth in labour supply constrains wage growth. A June cut remains mostly likely our view, but an April move is now back on the table.

Canada Consumer Price Index				
Period	2023M12	2024M01	2024M02	
All-Items				
Actual y/y %ch.	3.4	2.9	2.8	
Actual, m/m %	-0.3	0.0	0.3	
Seas. adj., m/m %	0.3	-0.1	0.1	
CPI by Select Product Group, y/y % ch.				
Exc. food and energy	3.4	3.1	2.8	
Goods	2.4	1.3	1.2	
Services	4.3	4.2	4.2	
Food	5.0	3.9	3.3	
Shelter	6.0	6.2	6.5	
Gasoline	1.4	-4.0	0.8	
Bank of Canada Core Measures, y/y % ch				
Common	3.9	3.3	3.1	
Trim	3.7	3.4	3.2	
Median	3.5	3.3	3.1	
3-mth trend, seasonally-adjusted (ann.)				
All-Items	2.3	1.8	1.3	
Exc. food and energy	3.6	2.4	1.3	

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