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TD Economics

Data Release: Canadian inflation smooth on the surface, hiding crosscurrents underneath

- Canadian inflation held steady in June at a 1.5% y/y pace. Ditto for the Bank of Canada's core inflation measure, which held at 2.1% (y/y).

- Not surprisingly given hot housing markets in parts of Canada, housing and related expenditures were key forces behind inflation. Over the past year shelter (+1.6%) and the household operations furnishings and equipment index (+2.8%) have had the biggest impact on headline inflation. Accelerating shelter costs in June were partly attributable to higher homeowners' replacement costs (+3.5% y/y). Housing-related durable goods like furniture and appliances have also seen hotter than average price increases, likely reflecting a weaker Canadian dollar driving up the cost of these largely imported goods.

- Canadians did get a break on their food bills, as food price inflation continued to ebb in June. Food prices were up only 1.3% over the prior year, down from a 4% pace earlier this year.

- Gasoline prices continue to put downward pressure on headline inflation in June, with prices at the pump 8.5% lower than a year ago. Unfortunately, within the transportation category (+1/1% y/y), savings on gasoline were offset by higher prices for passenger vehicles (+5.6%), due largely to the weaker Canadian dollar.

Key Implications

- On the surface, Canadian inflation has been a bit of a yawner in recent months. Core inflation has remained close to the Bank of Canada's target, while headline inflation is creeping up gradually as the impact of the past drop in energy prices is fading.

- Under the surface, however, there are a few notable trends reflecting the state of Canada's economy and the lower level of the loonie. Inflation for durable goods (cars, appliances, furniture) is running hot at 3.8% y/y, reflecting the higher level of imports in this category. Whereas inflation for services remains contained at 1.9%. Services inflation has cooled from 2.4% y/y in mid-2014 before Canada was hit by the oil-price collapse, as weaker domestic demand influences demand for services.

- Canada's economy continues to work through the difficult adjustment to the oil price collapse, as re-emphasized by the Bank of Canada last week. Today's inflation data doesn't change that narrative. The current stimulative stance of monetary policy is likely to remain warranted for quite some time.

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