Canada: Annual inflation decelerates for the first time in 13 months in July
By Jocelyn Paquet and Alexandra Ducharme

Coming in roughly in line with consensus expectations, headline inflation decelerated in July, with much of the monthly decrease stemming from lower gasoline prices. Other categories also contributed to the decline, such as transportation (biggest seasonally adjusted monthly decline since April 2020) and clothing/footwear (biggest since September 2020). However, food prices extended their stratospheric ascent and reached their fastest annual progression since 1982. Meanwhile, rent registered another strong monthly advance which translated into a 4.9% annual gain, the biggest since 1989, while mortgage interest costs jumped 1.7% from a month ago, the most since the early 1980s (left chart). Obviously, this was due to rising interest rates but, as these seem to have peaked, a slowdown is to be expected later this year. With fading demand in the real estate sector, we can also expect a moderation in homeowners’ replacement cost. Prices in this category were up only 0.1% in July, the smallest progression in two years. Meanwhile, the average of the three core measures preferred by the Bank of Canada increased in July, but mostly on an upswing in the CPI-common, whose methodology we questioned in one of our most recent special report. Given this, we recommend focusing on CPI-Trim and CPI-median, which have proved better at capturing underlying inflation trends. Encouragingly, our in-house replications of these measures are showing signs of slowdown, with 3-month annualized progressions dropping below 6-month gains (right chart). Although this suggests the worst is now behind us, inflation remains too high, which should encourage the Bank of Canada to implement a 75-bps rate hike at its September meeting. The situation will become more complicated after that, as growth is expected to slow, hampered by reduced global demand and a weakening housing market. In this context, further tightening of monetary policy could prove counterproductive, which leads us to believe that the Bank of Canada will then take a break and gauge the effects of the actions taken so far.

**Fastest monthly acceleration in mortgage interest cost since 1982**
Mortgage interest cost component of CPI inflation, monthly change (%), not seasonally adjusted

**HIGHLIGHTS:**
- Canada’s consumer price index rose a consensus-matching 0.1% in July (not seasonally adjusted) after a 0.7% gain the prior month.
- In seasonally adjusted terms, headline prices were up 0.3%, the smallest gain in 16 months. Higher prices for food (+0.7%), recreation/education/reading (+0.6%), alcoholic beverages/tobacco products (+0.6%), shelter (+0.4%) and health/personal care (+0.4%) were only partially offset by declines for transportation (-0.6%), clothing/footwear (-0.5%) and household operations/furnishings (-0.1%).
- Year on year, headline inflation weakened from a 40-year high of 8.1% in June to 7.6% in July.
- On a provincial basis, the headline annual inflation rate was above the national average in British Columbia (+8.0%), while it was in line with that mark in Ontario (+7.6%), Alberta (+7.4%) and Quebec (+7.3%), meanwhile, recorded lower annual inflation.
- On a 12-month basis, core inflation measures were as follow: 5.5% for CPI common (up two ticks vs. the prior month), 5.4% for CPI trim (down one tick) and 5.0% for CPI median (up one tick). As a result, the average of the three measures climbed from 5.2% to 5.3%, the highest level in the series going back to 1990.
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