

Another weak inflation print in May

Total CPI: Latest (y/y): +1.3% (actual); +1.5% (consensus expectations); +1.6% (previous)
CPI-Common: Latest (y/y): +1.3%; +1.3% (previous)
CPI-Median: Latest (y/y): +1.5%; +1.6% (previous)
CPI-Trim: Latest (y/y): +1.2%; +1.3% (previous)

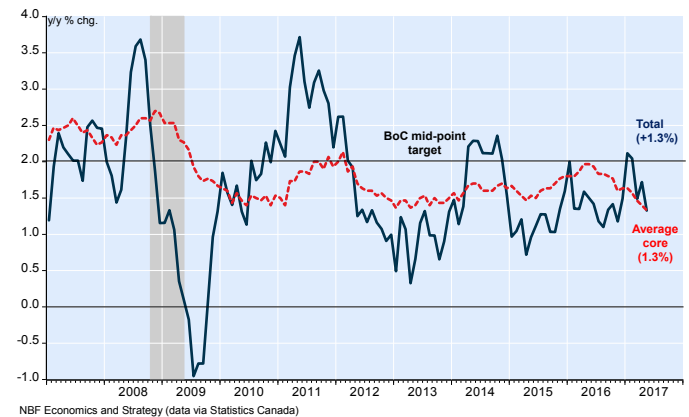
FACTS: Canada's consumer price index fell 0.2% in May in seasonally adjusted terms allowing the year-on-year inflation rate to drop three ticks to 1.3% (top chart). The advance was below consensus expectations calling for a 1.5% print. The reported increases in clothing (+0.6%), food (+0.3%), alcohol/tobacco (+0.3%) and household operations (+0.1%) were more than offset by declines in transportation (-1.1%), recreation (-0.3%), shelter (-0.1%) and healthcare (-0.1%). On a regional basis, all provinces experienced a decline in their annual inflation rate. The biggest drops were in Newfoundland & Labrador (3.0% from 3.6%) and Manitoba (1.0% from 1.6%). Alternatively, disinflation was less pronounced in Quebec (0.7% from 0.8%), British Columbia (1.9% from 2.1%) and Prince Edward Island (1.4% from 1.6%). CPI excluding food and energy rose 0.1% in seasonally adjusted terms pulling the year-on-year rate down one tick to 1.4%. On an annual basis, the CPI-trim stood at 1.2% (down from 1.3%), CPI-Median at 1.5% (down from 1.6%) and CPI-Common at 1.3% (unchanged).

OPINION: Inflation in Canada was below expectations for a fourth month in a row. Dropping gasoline prices restrained the progression of the headline figure and this should continue to be the case in June as excess supply is putting downward pressure on global oil prices. But what is more surprising is that underlying inflation remained weak in May. Indeed, CPI ex-food and energy posted a meagre 0.1% rise in the month allowing the annual rate to drop to 1.4%, its lowest level in more than 3 years. This weakness was entirely explained by the deflation in goods. Meanwhile, prices for services reflected a stronger domestic economy (middle chart). The measures used by the Bank of Canada to gauge underlying inflation were also weak in May. According to our in-house replication, both CPI-Trim and CPI-median rose a meagre 0.1% (bottom chart). As a result, the average of the three measures (CPI-Trim, CPI-Median, CPI-Common) stood at 1.3%, its lowest level in 17 years. While the economy is showing strong momentum, inflation remains particularly disappointing. Such a discrepancy is consistent with the fact that underlying inflation typically responds to the economic situation with a 3 to 5 quarter lag. For this reason, we still consider that the Bank of Canada will be justified to reverse the 2015 rate cuts before year end.

Matthieu Arseneau

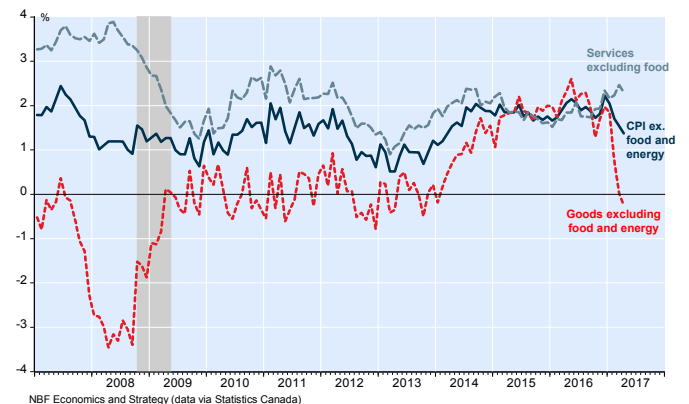
Canada: Perspective on the consumer price index

Total and average of the three core measures preferred by the Bank of Canada



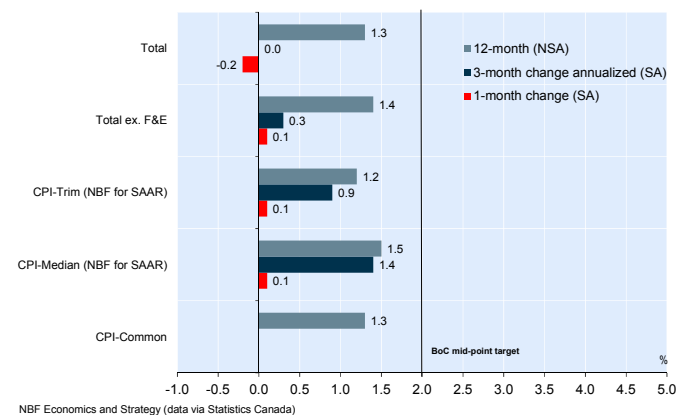
Canada: Goods are back in deflation

CPI ex-food and energy



Canada: Recent momentum of different inflation measures

CPI inflation (%)



Economics and Strategy

Montreal Office

514-879-2529

Stéfane Marion

Chief Economist and Strategist

stefane.marion@nbc.ca

Paul-André Pinsonnault

Senior Fixed Income Economist

paulandre.pinsonnault@nbc.ca

Krishen Rangasamy

Senior Economist

krishen.rangasamy@nbc.ca

Marc Pinsonneault

Senior Economist

marc.pinsonneault@nbc.ca

Matthieu Arseneau

Senior Economist

matthieu.arseneau@nbc.ca

Angelo Katsoras

Geopolitical Analyst

angelo.katsoras@nbc.ca

Kyle Dahms

Economist

kyle.dahms@nbc.ca

Toronto Office

416-869-8598

Warren Lovely

MD, Public Sector Research and Strategy

warren.lovely@nbc.ca

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