



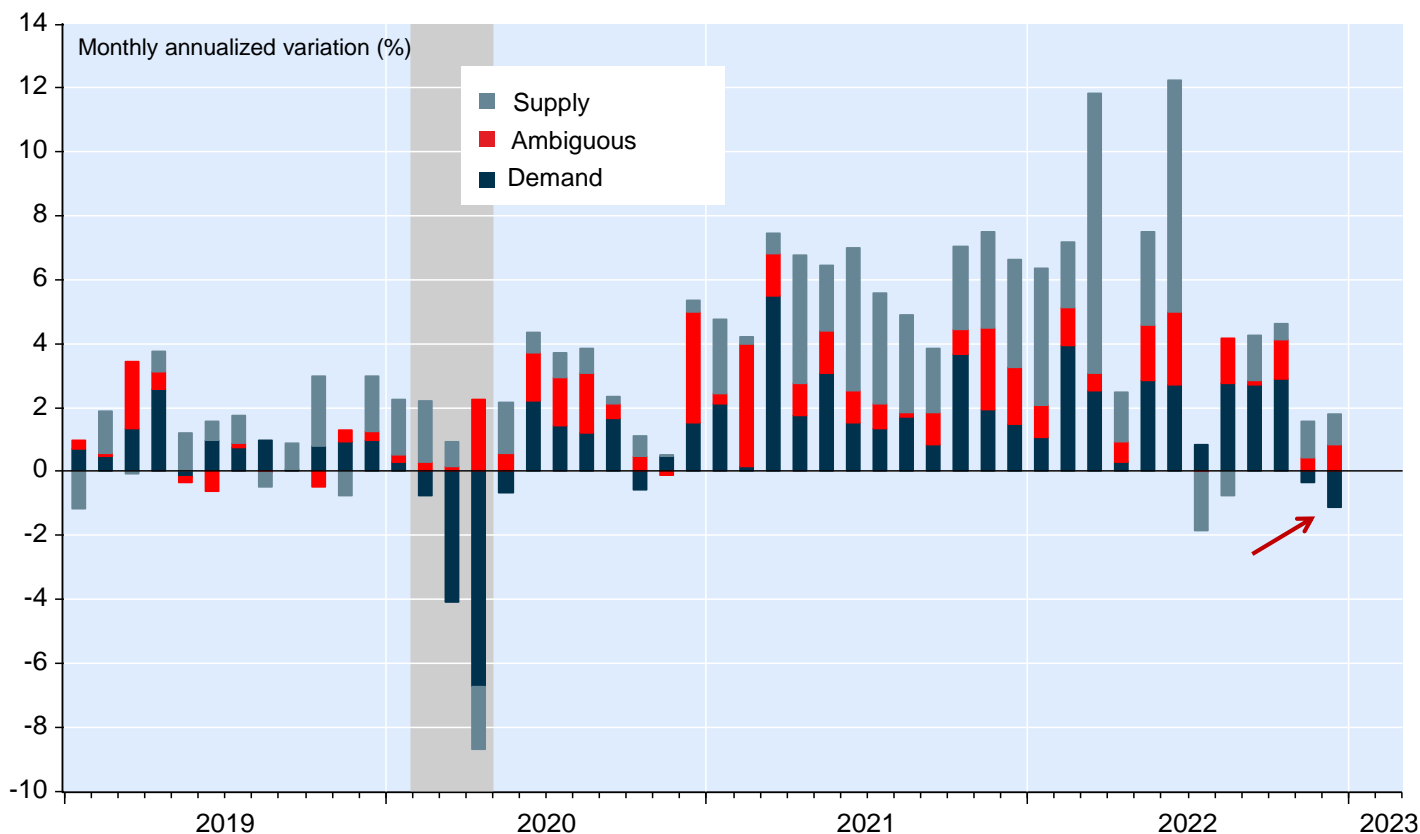
U.S. Watch

By Matthieu Arseneau and Alexandra Ducharme

While we eagerly await the Federal Reserve's interest rate decision this Wednesday, we got crucial developments on the inflation front Friday with December's reading of Personal Consumption Expenditure (PCE) inflation, the indicator the U.S. central bank targets according to its official mandate. The San Francisco Fed has developed a methodology to decompose PCE inflation into supply and demand components a few months ago, and the December decomposition has plenty to raise eyebrows. As today's Hot Chart shows, demand has been a negative contributor to U.S. inflation for two consecutive months now, a first since the initial pandemic shock. This development is consistent with volume consumption, which also recorded a second consecutive monthly decline in December, a first during this expansion. China's recent announcement to end its zero-covid policy and reopen its economy argues for a fading contribution from supply-driven inflation in the months ahead. With a resurgence in deflationary forces, we are confident that inflation will continue to come down faster than what is currently assumed by the Fed. What about the situation in Canada? In a [report](#) published last week, we used the methodology developed by the San Francisco Fed to evaluate the situation in our country and we noted the absence of demand-driven inflationary pressures in headline PCE in the third quarter, and a fading contribution of demand on the core figure. It will be interesting to monitor this situation when the data for the fourth quarter is available. We will keep you posted.

U.S. : Demand-driven inflation has vanished

Contribution of supply and demand to monthly annualized PCE deflator



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