



# Canada: December's CPI data ends a tumultuous year on a good note

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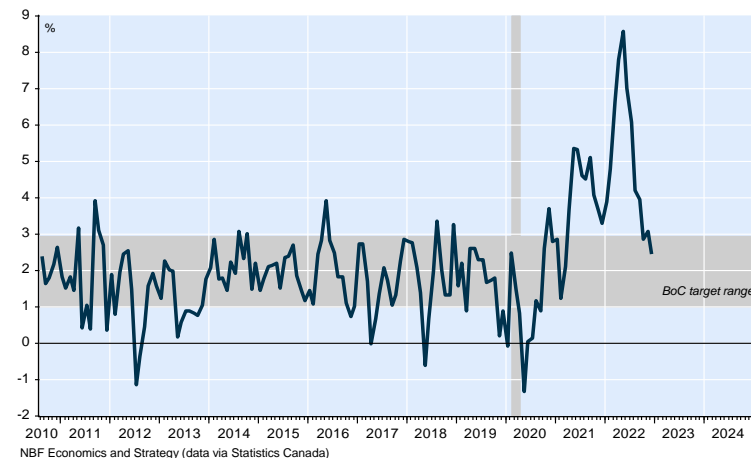
Inflation was dizzying in 2022, leading to an extremely rapid tightening of monetary policy. But the end of the year is offering hope that this inflationary surge will fade quickly in 2023. The spectacular drop in gasoline prices in December (-13.1%) has largely contributed to the monthly weakness, but other elements are also very encouraging, including the moderation of the food component. Excluding food and energy, m/m inflation came in at 0.28%, its lowest pace in 13 months, and would have been lower had it not been for the ongoing spike in mortgage interest costs (MIC), primarily due to central bank tightening. CPI excluding F&E&MIC is running at an annualized pace of 2.4% over the past three months, within the central bank's target range of 1% to 3% (left chart). The recent trend is also encouraging for the central bank's preferred measures, as evidenced by the three-month annualized change of 3.6% for the CPI-Trim and 4.3% for the CPI-Med, compared to over 7% earlier this year. This morning's data does not change our view that the Bank of Canada should consider a pause next week after the extremely aggressive tightening orchestrated in 2022 that brought real rates essentially back to pre-pandemic levels (right chart). Inflation in the last quarter of 2022 turned out to be 4 tenths lower than what the BoC projected last October (6.7% vs. 7.1%). In that same projection, the central bank saw inflation settling at 2.8% at the end of 2023, whereas we believe it will be below that level as early as the second quarter of the year. The actions taken so far will continue to dampen economic activity in the quarters ahead and, consequently, inflation. GDP and the labour market have remained healthy until the end of 2022, but the economic outlook is darkening according to the BoC's Business Outlook Survey. As many as 30% of corporations expect their sales volumes to decline, a record level outside of a recession. Higher inventories than before during the pandemic, significantly lower transportation costs, sales price reductions by Chinese producers and the global economic slowdown suggest that the lull on the goods side will continue. For services, the return to normal inflation levels may take a little longer, but there are reasons to believe that the labour market will ease in a low-growth environment, contributing to a reduction in wage pressures.

### HIGHLIGHTS:

- The Consumer Price Index decreased 0.6% in December, more than consensus expectations calling for a 0.5% pullback (not seasonally adjusted). This comes after a 0.1% increase the prior month.
- On a year over year basis, headline CPI dropped 5 ticks to 6.3%, below consensus expectations and its lowest level in 10 months.
- Excluding food and energy, m/m inflation stood at 0.28%, it's lowest pace in 13 months.
- In seasonally adjusted terms, headline prices were down 0.1%. Prices decreased in 3 of the 8 categories surveyed, namely transportation (-0.9%), household operations (-0.1%) and recreation/reading (-0.1%).
- Meanwhile, prices were up for clothing and footwear (+0.8%), health/personal care (+0.6%) and shelter (+0.4%), which was driven by a surge in mortgage interest costs (+2.7%). For its part, the price of food continues to moderate (+0.4%), which is still high on a historical basis, but the lowest of the last 6 months.
- Core inflation measures were as follow: 5.3% for CPI trim (down one tick from last month) and 5.0% for CPI median (also down one tick). As a result, the average of the two measures decreased from 5.3% to 5.2%.

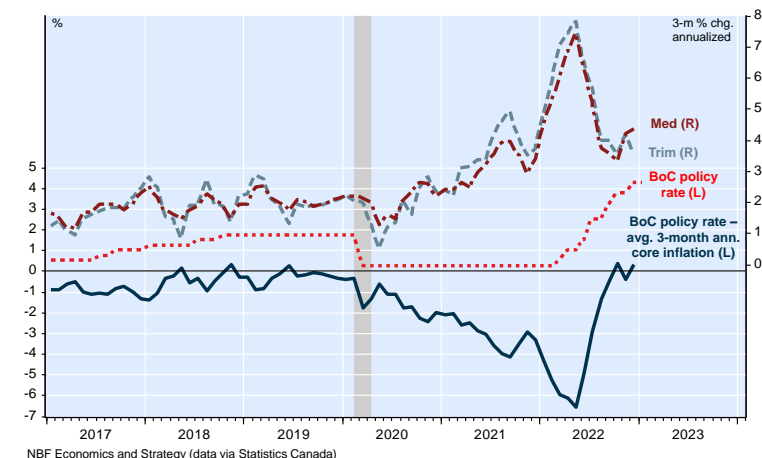
### Canada: Core inflation excluding MIC back to BoC's target range

3-month annualized change in inflation excluding food, energy and mortgage interest costs



### Canada: Real rates back to prepandemic levels

Nominal and real BoC policy rate and 3-month annualized measures of core inflation



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