RESEARCH BRIEF
CANADA INFLATION

IPA INSTITUTIONAL PROPERTY ADVISORS
A DIVISION OF MARCUS & MILLICHAP, BROKERAGE

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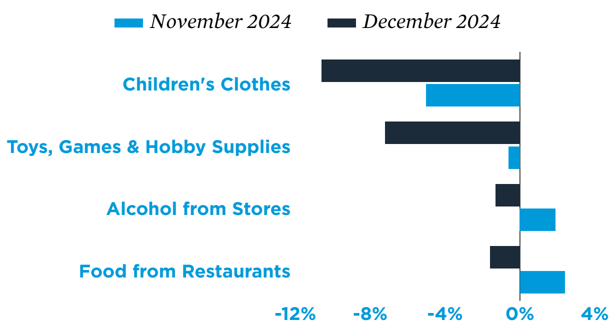
Inflation Remains Below Target Range, But Price Pressures Could Be Reaccelerating

Inflation inches lower amid government policy. Canada's headline inflation rate fell 10 basis points to 1.8 per cent in December, falling slightly short of market expectations that it would hold at 1.9 per cent. This reading marked the fifth consecutive month that inflation has sat at or below the Bank of Canada's target of 2.0 per cent. However, because the prices used in the Consumer Price Index are inclusive of all excise and other taxes paid by consumers, December's deceleration was largely fuelled by the ongoing GST tax holiday. In contrast, it appears previous interest rate cuts are causing underlying price pressures to reaccelerate. While the BoC's preferred CPI-trim and CPI-median measures of core inflation – which use tax-adjusted price data – eased on a year-over-year basis, the three-month annualized rate of these two measures accelerated to 3.5 per cent. Though this is unlikely to prevent a further rate cut this month, it is a trend the central bank will continue to monitor.

Further monetary easing still expected. Although underlying price pressures are creeping up, money markets still heavily favour another rate cut at the central bank's January meeting. With the GST tax holiday continuing until mid-February, inflation is likely to remain muted. Additionally, the threat of U.S. tariffs hanging over the economy should drive the need for a more accommodating interest rate environment, as protectionist trade policies will negatively impact Canada's economic growth. The BoC Governor had said last month that further rate cuts would be gradual, though, suggesting the monetary authority will return to a 25-basis-point cut in January.

Prices Included in Tax Holiday Drop

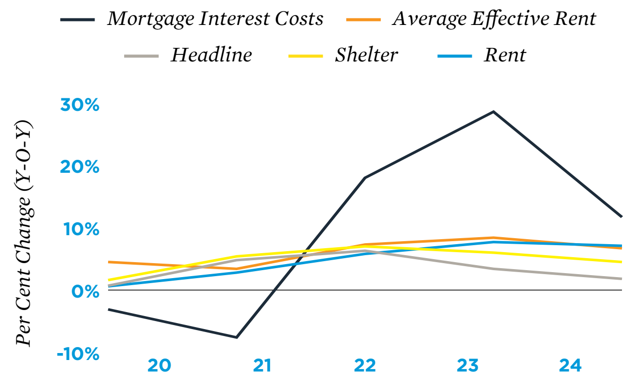


Commercial Real Estate Outlook

Shelter costs continue to ease. Housing has been a primary driver in headline inflation. Since the start of 2022, mortgage interest costs were up 70 per cent as of December, while rent had jumped 21 per cent. Yet, overall shelter inflation – which peaked at 7.4 per cent in 2022 – has been cooling, rising 4.5 per cent year over year in December. The mortgage interest cost index has already decelerated for the sixteenth consecutive month, and compared with November, rent inflation in December dropped 60 basis points to 7.1 per cent. This trend is expected to continue as lower borrowing costs feed through into the broader economy. Not only are less restrictive interest rates enabling some renters to transition into homeownership, but historic apartment deliveries and tighter immigration policies are allowing some balance to return to the market. This is consistent with Canada's multifamily performance. In 2024, the national apartment vacancy rate jumped 70 basis points to 2.2 per cent, causing annual rent growth to soften 160 basis points to 6.7 per cent.

Travel more expensive. Prices for traveller accommodations rose 13.6 per cent year over year in December 2024, reflecting a solid year of hotel performance. Occupancy rose marginally, and growth in key revenue metrics exceeded 4.0 per cent. Looking ahead, though some demand tailwinds remain, early forecasts suggest a moderation in performance as supply growth outpaces demand. Nevertheless, a more friendly monetary environment will likely boost discretionary spending, while a weakening Canadian dollar will influence domestic travel and attract U.S. visitors. This will help maintain average daily rate growth around the pace of inflation.

Housing a Key Driver in Inflationary Pressures



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Sources: IPA Research Services; Altus Data Solutions; Bank of Canada; Canada Mortgage and Housing Corporation; Capital Economics; CoStar Group, Inc.; Statistics Canada