RESEARCH BRIEF
CANADA INFLATION

IPA INSTITUTIONAL PROPERTY ADVISORS
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Inflation Accelerates Amid Policy Change, While Tariffs Cloud CRE Outlook

Underlying pressures mount. Inflation rose 2.6 per cent in February, up from a 1.9 per cent increase in January and well above the consensus of a 2.2 per cent jump. Price acceleration was broad-based, as inflation inched higher in six out of eight components. Lower interest rates are now feeding through into stronger household consumption, hitting 5.6 per cent annualized in the fourth quarter of last year. The end of the GST tax break partway through the month also contributed notable upwards pressure to prices for eligible products. Yet even when removing the tax implication, underlying price pressures are accelerating. Both of the central bank's measures of core inflation jumped 20 basis points to 2.9 per cent – or a three-month annualized rate of 3.3 per cent – reinforcing a trend that began to emerge over the latter parts of last year. Amid ongoing uncertainty stemming from a looming trade war, the Bank of Canada will have to balance reaccelerating price pressures with downside risks to economic growth.

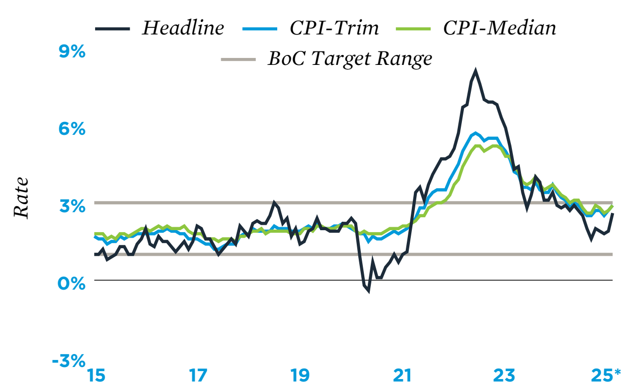
Rate pause now a more likely outcome. Despite growing inflation pressures and strong fourth quarter GDP numbers, Canada's central bank cut its overnight rate by 25 basis points to 2.75 per cent at its March policy meeting, as it looked to position Canada's economy for tariff uncertainties. Looking ahead, however, swap markets are now placing a nearly 70 per cent chance of a rate pause at the Bank's April announcement. Not only are price pressures mounting, but reciprocal tariffs on U.S. imports could push prices up further and create a stagflation environment. Major banks are still penciling in further cuts, but the timing and the terminal rate are now less predictable.

Commercial Real Estate Outlook

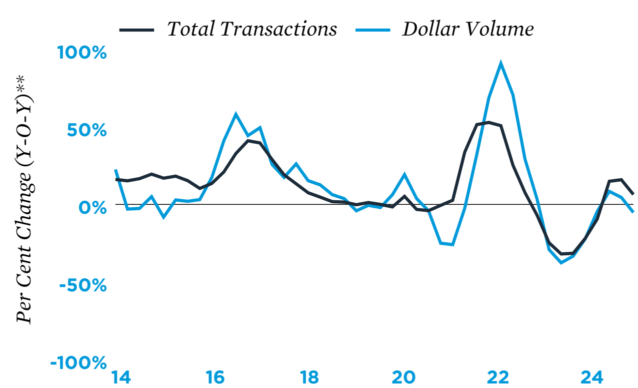
Investors monitor market dynamics. Heading into 2025, economic and commercial real estate investment indicators were turning positive. Lower interest rates were generating economic momentum and supporting improving property fundamentals, while also bolstering investor confidence, helping deals pencil. As a result, investment activity was rising; however, the sales recovery may now be more gradual than first thought. Lower interest rates should still help facilitate deals, but tariff uncertainties, as well as the wind down in monetary easing, could prompt some investors to become more cautious.

Inflation reflects preferred investment options. In February, a 5.8 per cent jump in rent inflation and a 2.8 per cent rise in food purchased from stores inflation outpaced the headline rate of 2.6 per cent. Though the pace of growth for these categories has been easing over the past year, February's readings highlight ongoing demand for essential products like housing and food. At the same time, property fundamentals for apartment rentals and retail have been sound, tending to show more resilience in times of economic uncertainty. While up 70 basis points from 2023, Canada's multifamily vacancy rate ended last year at 2.2 per cent, helping to drive annual rent growth of 6.7 per cent. Meanwhile, retail vacancy hit an all-time low of 1.5 per cent, supporting annual rent growth of 3.3 per cent. Looking ahead, these sectors do face some demand uncertainties amid tighter immigration policies and ongoing trade headwinds. Nevertheless, supply constraints and their essential nature will likely preserve the property types as preferred investment options.

Inflation Pushing Closer to Upper Range Bound



Investment Recovery Stalls Amid Uncertainties



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** Through February; ** Four-quarter moving total*
Sources: IPA Research Services; Altus Data Solutions; Bank of Canada; Canada Mortgage and Housing Corporation; Capital Economics; CoStar Group, Inc.; Statistics Canada