RESEARCH BRIEF
CANADA INFLATION

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

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Core Pressures Accelerate, Yet Removal of Carbon Tax Curbs Headline Rate

Inflation reading offers a mixed bag. The removal of the consumer carbon tax caused energy prices to fall sharply in April, pushing the headline inflation rate down 60 basis points to 1.7 per cent. Despite this, underlying price pressures continued to mount. When stripping out energy, the consumer price index rose 2.9 per cent year over year — up from a 2.5 per cent reading in March. Additionally, the Bank of Canada's preferred measures of core inflation, CPI-trim and CPI-median, jumped 0.4 per cent month over month, causing the average three-month annualized rate to accelerate to 3.4 per cent. Motor vehicle parts were one of the main categories putting upwards pressure on core inflation, potentially due to retaliatory tariffs implemented at the start of the month. Food prices also rose by a strong 0.5 per cent monthly rate, which again could reflect trade pressures.

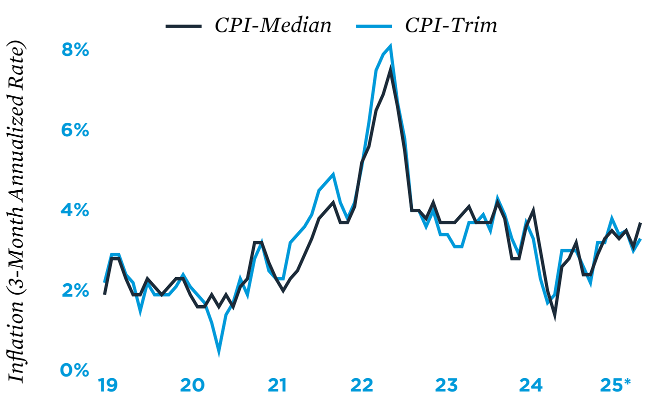
Further easing now a coin flip. Prior to April's inflation release, money markets were pricing in a 65 per cent chance of a June rate cut. After the release, that probability fell to roughly 45 per cent. That said, Canada's central bank has made some dovish statements in recent months. It appears they are more concerned about downside risks to the economy stemming from ongoing trade uncertainties and slowing global economies. As a result, many economists are still penciling in a June cut, especially as weakness begins to form in Canada's labour and housing markets, as well as in its manufacturing output. Terminal rate forecasts now range between 2.0 per cent and 2.25 per cent, with money markets leaning towards the latter.

Commercial Real Estate Outlook

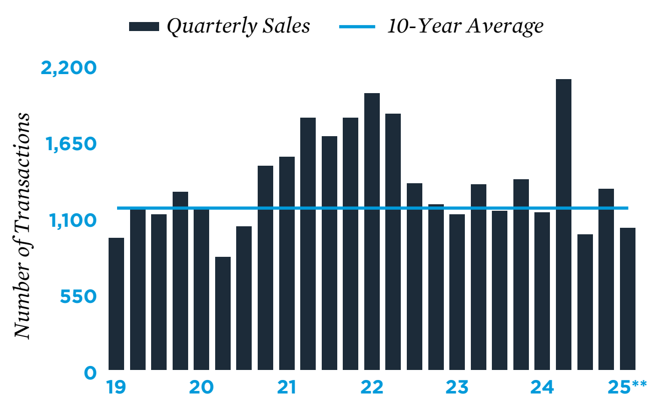
Investors have a swath of information to consider. Heading into 2025, Canada's economy and commercial real estate investment market were gaining momentum. Annualized GDP growth largely trended up over the course of last year. The total number of transactions among major commercial property types also began to turn a corner, as lower interest rates and healthy fundamentals were driving investor optimism. Since then, however, ongoing uncertainties have curbed momentum. GDP growth is now forecast to slow notably to below 1.0 per cent annualized over the course of 2025. Meanwhile, CRE investors pulled back in the first quarter of the year amid a 20 per cent quarterly drop in the total number of sales. Although fundamentals largely remain healthy, and stabilizing borrowing costs — as well as more attractive price points — could offer a favourable entry point for investors with a long-term strategy, ongoing uncertainties could dampen the expected CRE investment recovery.

Higher costs could impact retail property sector. Some inflation is not necessarily bad for retailers. It usually reflects strong consumer demand and increased sales. The current environment, however, poses some risks. While growing economic momentum over last year was encouraging, pressures are starting to mount amid ongoing trade headwinds with China and the United States. Not only have recent tariffs increased input costs for retailers, but they have also curbed consumer confidence. Retail property sector fundamentals could soften this year as a result. Nevertheless, limited supply is forecast to keep vacancy well-below equilibrium, remaining around 2.0 per cent.

Underlying Inflation Pressures Mount



Uncertainty Halts CRE Sales Momentum



* Through April; ** Through 1Q
Sources: IPA Research Services; Altus Data Solutions; Capital Economics; CoStar Group, Inc.; Statistics Canada