Research Brief

CANADA INFLATION

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IPA | INSTITUTIONAL PROPERTY ADVISORS

A DIVISION OF MARCUS & MILLICHAP, BROKERAGE

Underlying Inflation Trend Supports Stable Rate Outlook and CRE Recovery

Temporary factors push inflation higher. Canada's consumer price index rose 0.3 per cent in July, lifting the annual inflation rate back to 3 per cent. Higher gasoline prices accounted for roughly half of the monthly increase, while temporary pressures also emerged in communications, airfares, and travel services. FIFA World Cup activity contributed to higher travel-related costs, while the timing of promotional events likely influenced prices for household goods and textiles. These pockets of price pressures also pushed the Bank of Canada's preferred core measures higher during the month. However, their average annual rate remained at the Bank's 2 per cent target, suggesting underlying inflation pressures remain relatively contained.

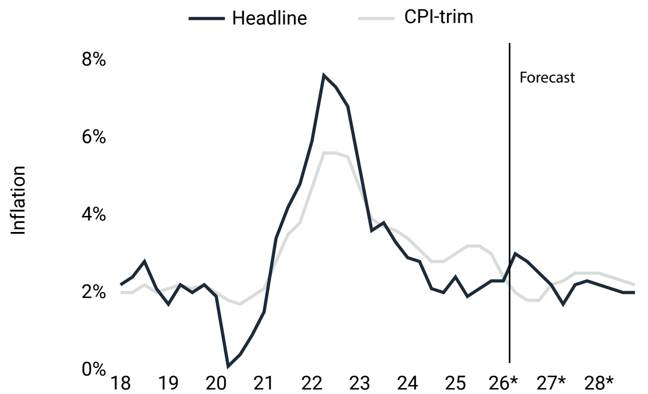
Inflation outlook supports an extended rate hold. July's stronger inflation reading is unlikely to alter the Bank of Canada's interest rate outlook, particularly as many of the month's largest price increases appear temporary. Gasoline inflation should moderate alongside energy markets, while World Cup-related travel pressures and one-off increases across communications and household goods will likely recede. This relatively benign underlying inflation backdrop continues to offset stronger economic and labour market data, reducing the need for either additional monetary support or near-term tightening. As a result, the Bank is likely to keep its overnight rate unchanged at 2.25 per cent through the rest of the year, although rising bond yields and their impact on mortgage interest costs remain an upside risk.

Commercial Real Estate Outlook

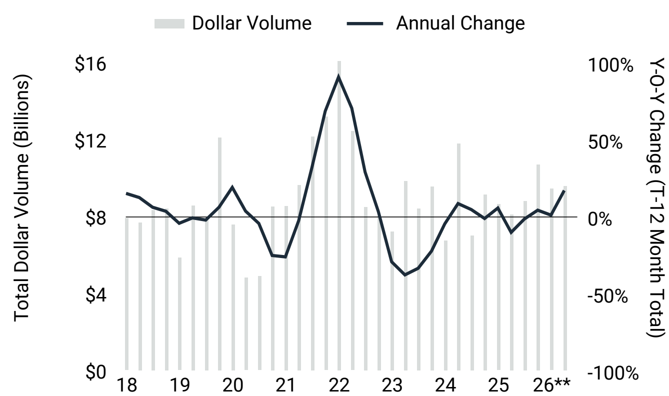
Improving capital market conditions support investment activity. Greater interest rate stability, improved price discovery, and sound fundamentals are helping bring investors back to Canada's commercial real estate market. On a trailing 12-month basis, investment volume reached $38.4 billion, approximately 17 per cent above the comparable period a year earlier and the strongest pace since 2022. While borrowing costs remain elevated and bond yields have experienced periodic volatility, greater clarity on valuations, along with commercial real estate's income-producing and defensive characteristics, should support continued improvement in transaction activity.

Hospitality benefitting from strong operating fundamentals. Hotels entered the second half of 2026 on solid footing, supported by limited supply growth and continued pricing power. RevPAR increased 6.5 per cent during the first half of the year, driven primarily by a 6.2 per cent jump in average daily rates. Occupancy also improved as supply grew by just 0.6 per cent. Strong performance and a restrained development pipeline continue to attract capital, with approximately $1.1 billion of hotel assets trading over the past 12 months and cap rates stabilizing in the high-8 per cent range. Despite elevated financing costs, healthy domestic travel demand, limited new supply, and improving capital market conditions should support both operating performance and hotel investment activity throughout the rest of the year.

SPIKE IN INFLATION APPEARS TO BE TEMPORARY



CRE INVESTMENT SLOWLY GAINING MOMENTUM



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* Through 2Q 2026, forecast thereafter; ** Through 2Q | Sources: Altus Data Solutions; Capital Economics; CoStar Group, Inc.; Oxford Economics; Statistics Canada