

October 6, 2026

Canada-US inflation risks: One of these things is not like the other

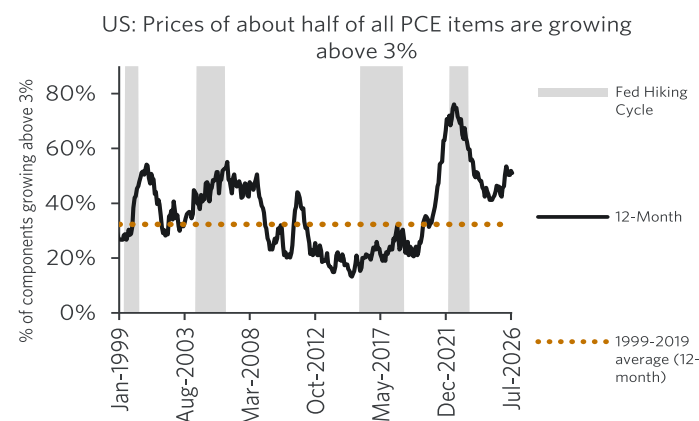
by Helen Lao helen.lao@cibc.com

When the Federal Reserve delivered the 25bps rate hike two weeks ago, they phrased it as a move to “support a timelier return to the Committee’s 2% goal.” The knee-jerk reaction in Canadian markets was to assume that the Bank of Canada would soon follow. It’s a fair instinct, as the two economies are facing the same energy supply shock that is pushing up total inflation. But look past the headline decision and at what’s driving it, and the case for a parallel Canadian hike at this moment gets much weaker. Simply put, the underlying inflation picture and the risk that CPI will be “stuck” above target, just isn’t the same between the two countries.

The breadth of inflation is wider in the US

At the Jackson Hole conference at the end of August, as well as the recent FOMC press conference, Fed Chair Kevin Warsh mentioned a key indicator he looks at to gauge underlying inflation: the share of more than 100 disaggregated components of PCE inflation that are rising above a 3% pace. About half of all PCE categories are currently outpacing that 3% rate on a 12-month basis. While that’s below the pandemic high of more than 70%, it’s nearly 20 percentage points above the norm in the decades of quiet inflation prior to the pandemic (Chart 1).

Chart 1: Half of all PCE items in the US are growing above 3% on an annual basis



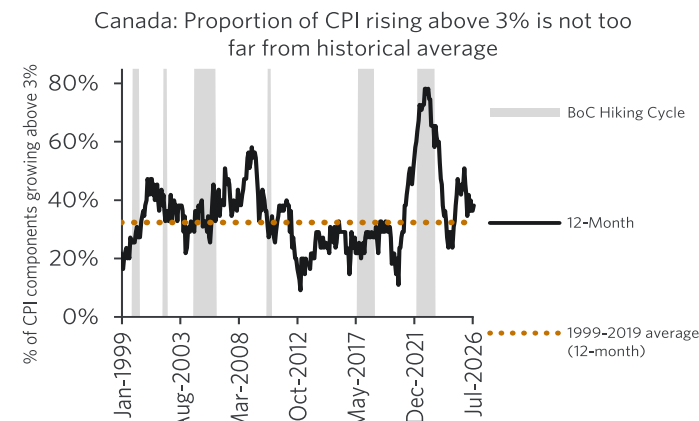
Sources: BEA and CIBC

In Canada, inflation is much less broad-based. If we look at all 55 major subcomponents of CPI, we will see that only 38% of CPI components are rising at greater than 3% on a 12-month basis, a mere 6 percentage points above the historical average from 1999 to 2019 (Chart 2).

Gasoline prices are up in both countries, but contributions to inflation are not the same

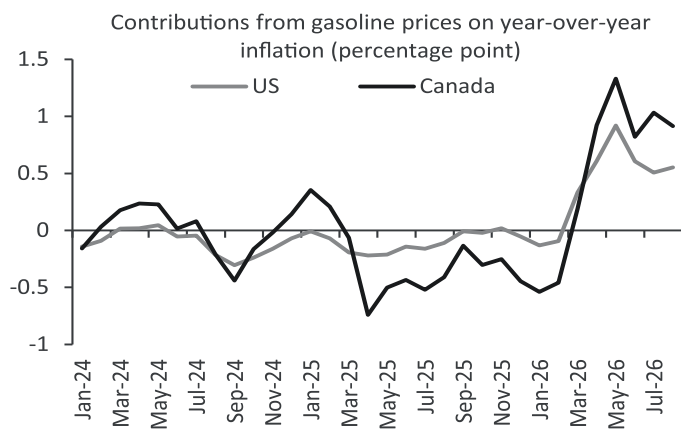
Since the beginning of the Iran conflict, gasoline prices have increased in both Canada and the US, but the climb has been slightly less aggressive in Canada. Regular unleaded pump prices in the US had gone up by 26% as of August relative to average 2025 prices. Looking at the estimated breakdown of components that make up gasoline prices at the pump, while the crude cost component has increased by about the same amount as the total pump price, the refining margins component has doubled. North of the border, Canadian regular gasoline prices had increased by about 21% as of August relative to average 2025 prices, the crude oil cost component had increased about 30% while the refining margins had increased by about 65%. Lower taxes helped to partially offset the increases from crude oil costs and refining margins in both countries. Importantly, refining margins have gone up more than crude oil costs for both countries since the Iran

Chart 2: Proportion of CPI items rising above 3% in Canada is not too far from historical average



Sources: Statistics Canada and CIBC

Chart 3: Gasoline contribution to total inflation is higher in Canada than the US



Sources: Statistics Canada, BEA and CIBC

war because refined-product supply has been much more constrained than crude supply.

Although gasoline prices have increased slightly more in the US than Canada, its contribution to total inflation is still lower because its weight in total PCE (about 2%) is smaller than the weight in total CPI in Canada (4%). As of August, gasoline is contributing 0.5 p.p. to total PCE inflation in the US while it is contributing 0.9 p.p. to total CPI inflation in Canada (Chart 3). The result is that, should gasoline prices begin to abate, it could represent a more meaningful cure for headline inflation north of the border.

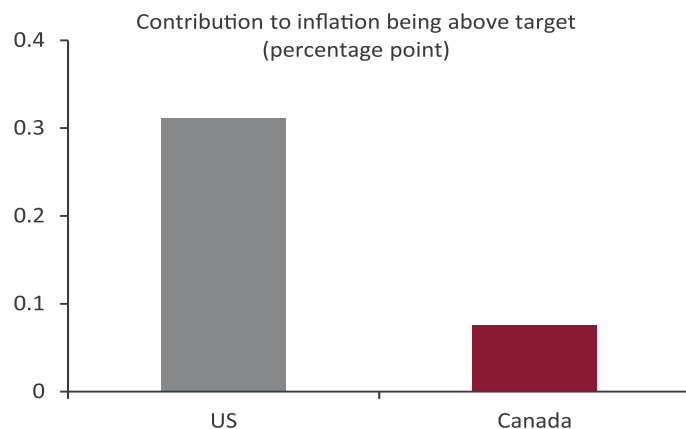
AI and tariffs also feeding into the US-AI and tariffs also feeding into the US-Canada inflation gap

As detailed in an earlier article ([Quantifying the AI hit to US inflation](#)), we estimate that the direct impact from higher information processing equipment prices (including computers, software and accessories) is about 0.3 p.p. as of August. In Canada, computer equipment, software and supplies prices are also rising rapidly at 8.4% year-over-year as of August, which implies that its contribution to total CPI is above its historical average. We attribute this to the impact from strong AI-demand, and this accounts for about 0.1 p.p. of CPI inflation being above target, which is less than the estimated US impact (Chart 4).

The tariff shock has also landed far more heavily on US consumers than on Canadians. A recent St. Louis Fed study found that tariffs currently contribute about 0.6 p.p. to total PCE inflation being above target in the US. In Canada, the newly enacted counter-tariffs are expected to boost inflation by about 0.2 p.p. in the coming months.

Helped by AI capital spending and less of a tariff hit to its exports, the American economy is also running hotter than Canada's. The US output gap, or excess demand, is currently estimated to be around 1% of GDP, which roughly translates

Chart 4: AI is contributing more to inflation above target in US than Canada



Sources: Statistics Canada, BEA and CIBC

into a 0.2 p.p. boost in the annual pace of PCE inflation¹. In contrast, Canada, facing a greater tariff hit to exports, and benefiting less from AI spending, so is currently in excess supply. That slack is estimated to represent a 0.2 p.p. drag on inflation.²

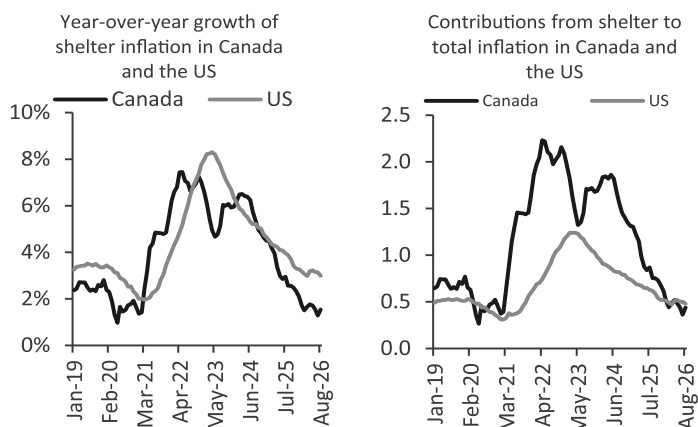
Shelter costs decelerating in both countries with similar contributions to inflation

Housing inflation has been decelerating on a year-over-year basis in both Canada and the US. While the US pace is currently running higher than Canada (Chart 5, left), the contributions to total inflation are not too different between the two countries (Chart 5, right). That is because the weight of shelter is much bigger in total inflation in Canada (about 25% of total CPI basket) than in the US (about 15% of total PCE).

¹ Based on estimate from Jorgensen, P.L., & Lansing, K.J. (2021, August 9). Return of the original Philips curve. FRBSF Economic Letter, 2021-21.

² Based on contributions of output gap on year-over-year CPI inflation in 2026Q2 and 2026Q3 from Bank of Canada's July Monetary Policy Report.

Chart 5: Shelter inflation is decelerating on an annual basis in both Canada and the US and their contributions to total inflation are similar



Sources: Statistics Canada, BEA and CIBC

Gasoline drives most of above target inflation in Canada; the US has broader worries

While inflation is above target on both sides of the border, only in Canada is that almost all a story of gasoline prices, which could abate if geopolitical events improve global crude supply. CPI inflation in Canada is currently about 1 p.p. above the 2% target while PCE inflation in the US is about 1.4 p.p. above target. But in Canada, almost all of the above target inflation is due to higher gasoline and potential spillover effects. As of August, about 0.8 p.p. of the 1 p.p. gap to the 2% CPI target is attributable to higher than average gasoline prices. Higher gasoline prices also spill over to higher airfares and travel tours, and that explains about 0.3 p.p. of CPI above target. The disinflationary effect of economic slack partly offsets these impacts (Chart 6).

Crude oil futures are currently building in expectations for an easing in oil prices over the coming year. While refining margins are also elevated and contributing to gasoline and diesel costs, the overall contribution to the 12-month inflation rate will diminish as we lap elevated prices that showed up in the winter.

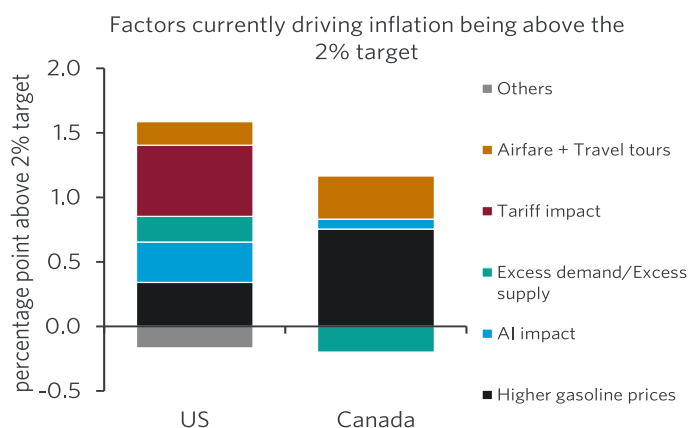
In contrast, only 0.3 p.p. of the larger US gap to its PCE target of 2% is coming from higher gasoline prices (Chart 6). The potential spillover to higher airfare prices accounts for another 0.2 p.p. Combined, these account for 0.5 p.p. of the 1.4 p.p. above target PCE inflation in August. Tariff and AI impacts, explain much more (about 0.9 p.p.) of the above target inflation in the US.

As a result, the risk that inflation is persistently stuck above the 2% target appears greater in the US than in Canada, both due to the greater breadth of its inflation issues, and the fact that only the American economy is overheated relative to potential

GDP. In Canada, while we will see a small lift to CPI from newly imposed tariffs, any cooling in fuel costs will go a long way to getting inflation back to target. Even if pump prices decelerate only gradually, the risk that energy costs spill over into broader inflation pressures should be lower in Canada given the current degree of economic slack, particularly if economic growth eases off in Q4 as new trade frictions bite.

The Fed is likely to raise interest rates once more in order to cool demand and bring inflation back down. Canada could follow suit in 2027. But the timing of its rate hike decisions will be a made-in-Canada story that will reflect not only its more favourable starting point on underlying inflation, but also the potential challenges to growth in the face of elevated US tariffs and trade uncertainties ahead.

Chart 6: Higher gasoline prices is the dominant driver for above target inflation in Canada, the US has broader worries



Sources: Statistics Canada, BEA and CIBC

Note: Impact of airfare, travel tours and higher gasoline prices are their current contributions minus historical average contribution when inflation average 2% in Canada and the US.

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