It’s been a bit of a mystery. Inflation has been so persistently low, not just in Canada but also in other countries, that central bankers are not only trying to push it up, but also struggling to explain why it isn’t higher.

Consumer price inflation has averaged just 1.5 per cent annually since 2008, even though central banks want inflation to be higher. An average of 1.5 per cent is well below the Bank of Canada’s two per cent target rate of inflation.

As Claudio Borio, head of the monetary and economics department of the Bank of International Settlements, recently stated:

> *“Central banks must feel like they have stepped through a mirror, and who can blame them? They used to struggle to bring inflation down or keep it under control; now they toil to push it up. They used to fear wage increases; now they urge them on. They used to dread fiscal expansion; now they sometimes invoke it. Fighting inflation defined a generation of postwar central bankers; encouraging it could define the current one.”*

Why would central banks want inflation to be higher? One reason is to lessen the threat of deflation (ongoing declines in prices) as happened during the Great Depression. Deflation can be far more damaging than inflation. Higher inflation, if accompanied with higher wages, could also improve the financial situation of households and provide central banks with more ability to act in the future.

Many of the factors that have kept wage increases low, such as globalization and the information technology revolution, also appear responsible for keeping inflation low, and could restrict price increases over the long term. It may also be that it's taking inflation longer to materialize. With the economy tightening, the Bank of Canada expects consumer price inflation to move up to two per cent in the second half of 2018 and to remain close to that thereafter.

While economists and central bankers may struggle to understand what's affecting overall inflation, ordinary Canadians are getting hit with price increases that will hurt lower- and middle-income households the most.

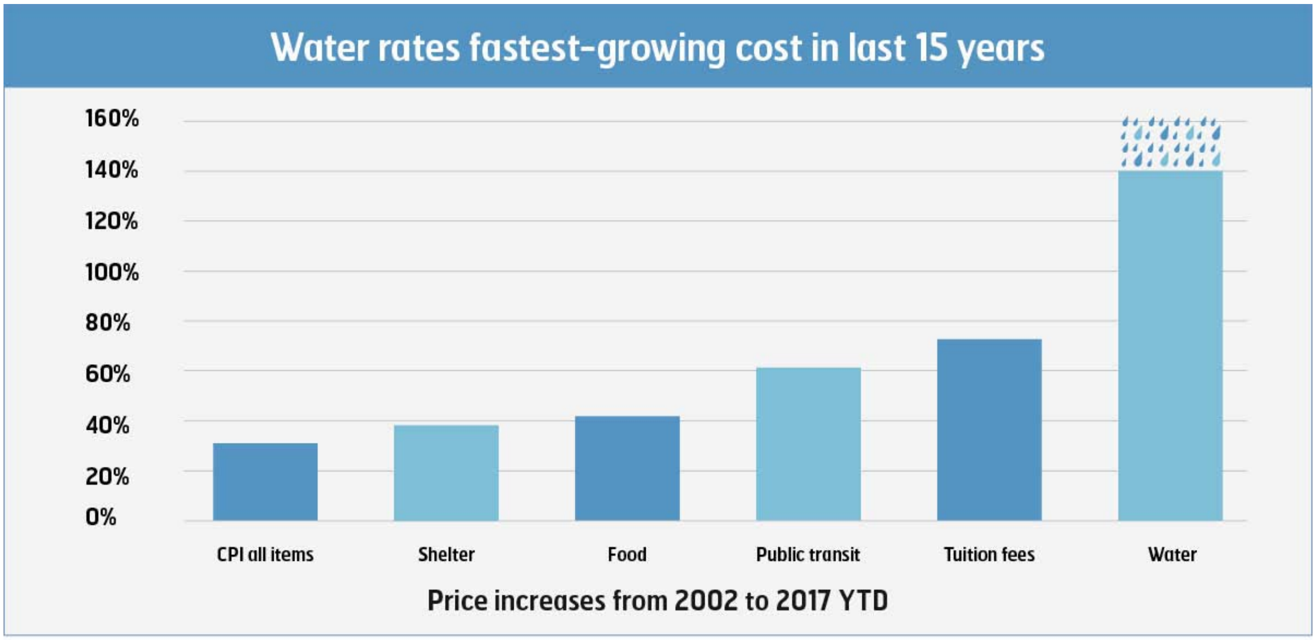
Swings in energy and food prices cause the greatest variation in consumer price inflation. They affect lower- and middle-income families the most, and have increased at a higher rate than overall consumer prices over the past 15 years.

While housing prices have escalated, low interest rates have kept homeowners' mortgage interest costs more affordable. That will change as mortgage rates increase, following Bank of Canada interest rate hikes. A full percentage point increase in mortgage rates will increase mortgage payments by about $50 per month or $600 per year for each $100,000 borrowed, amortized over 20 years.

Other costs that have persistently increased in recent years are the fees governments charge for public services, including for water, tuition, public transit and community sports and recreation services. All these fees have increased considerably more than overall prices, as governments shift more of the costs onto users and off the general tax base. Increased prices charged for water in some jurisdictions are no doubt being used to subsidize lower taxes.

In fact, fees charged for water have increased on average by more than any other individual component of the consumer price index over the past 15 years. Nationally, they've averaged a six per cent increase every year, adding up to a 141 per cent increase over 15 years. Rates charged for water have increased the most in Saskatchewan and Ontario, and the least in Quebec, where they've actually declined.

We may not know what's causing overall inflation, but it's clear what's causing some prices to increase—and it's in areas that will continue to pinch working families the most.



Source: Statistics Canada Consumer Price Index Cansim Table 326-0020