

WEEK ENDED JULY 18, 2025

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## Inflation – Deferred or Denied?

*“When business or an individual spends more than it makes, it goes bankrupt. When government does it, it sends you the bill. And when government does it for 40 years, the bill comes in two ways: higher taxes and inflation. Make no mistake about it, inflation is a tax and not by accident.”*

– Ronald Reagan

**The Through Line:** After years of being so low it could largely be ignored, inflation is once again headline news. This week’s readings of several key yardsticks, plus a bevy of bank earnings and more tariff news, give us the perfect opportunity to do a deeper dive into the topic – outlining what matters, what doesn’t and how best to interpret the impacts on economic activity.

### What is inflation and can it ever be good?

Inflation is typically framed as a *persistent* increase in prices versus a *one-time* reset. Given that rising prices mean falling purchasing power, most people jump to the conclusion that inflation is bad. FULL STOP. And it’s true – sharp increases in prices can be problematic, particularly if they are broad based, sudden and *especially* if sustained. Episodes of inflation can jar psyches and prompt a host of unpredictable behaviors that disrupt economic activity.

**Moderate inflation, however, is arguably healthy for an economic system because it allows companies a modicum of pricing power and the ability to move wages higher over time.** It also facilitates cost-of-living increases in fixed-rate support systems such as pensions and social security and keeps an economy away from deflation. While zero inflation may seem intellectually appealing, zero is perilously close to negative. This can entrench consumer behavior in a mentality of waiting for lower prices, which in turn can restrain growth. Japan – where a generation of workers did not receive salary increases up until the last year or two – is a real-life example of the consequences of an extended period of ultra-low inflation.

Central bankers in developed markets spent much of the period post-GFC to 2020 trying to coax inflation UP to a target of 2%. Their goal was to facilitate GDP growth and avoid stagnation. The steep acceleration in prices during and after the COVID-19 pandemic in 2020 has thrown everyone for a loop trying to figure out how to get the inflation genie back in the proverbial bottle (chart). It has also left many wondering what the normal neutral, central-bank policy rate (often referred to as the terminal rate) will be after all the recent tests are more settled. Central banks’ policy rates are often a reference point for where inflation heads – and how consumers and businesses think about future levels.

Sticky-Price Consumer Price Index less Food, Energy



As of June 2025. Gray bars indicate U.S. recessions.  
Sources: Federal Reserve Bank of Atlanta, Sticky Price Consumer Price Index less Food and Energy via FRED (2025), Bloomberg L.P. (2025)

### How do I measure thee? Let me count the ways

Inflation is measured using an army of statistics. In the U.S., for instance, data is parsed broadly by time period (month over month, year over year), by category (goods, services) and by those experiencing the change (producers or consumers) to name just a few measures. Statistics can be gathered by survey (Survey of Consumer Expectations, Purchasing Managers, Philly Fed) or by actually counting price changes in widgets (CPI or PPI). Inflation can be further sliced into “headline” (all components of a particular indicator), “core” (removing volatile food and energy so if you don’t eat or heat you’re golden), and even “super core” (which also removes housing costs). Basically, there is a data set or subset to support whatever narrative a strategist wants to tell. However, themes and trends across and within each set often weave together to provide critical information about inflation’s timing and direction.

## Great expectations

**The absolute level of inflation in a given period matters less than the rate consumers and businesses expect to see in the future.** For example, if consumers assume prices will continue to rise aggressively they might push employers harder for wage increases, inciting a wage/price spiral. On the other hand, if they anticipate lower prices they might delay purchases, negatively weighing on growth. For this reason, the Fed's rate-setting body, the FOMC, continually surveys sentiment and activity of the entities within its various regions then compiles the insight-laden Beige Book (published eight times a year). The Fed also closely monitors sentiment and future expectations through economic indicators such as the University of Michigan Consumer Sentiment Index. The Bank of Canada conducts similar sentiment reviews via its Business Outlook Survey.

Capital markets collectively curate their own expectations of future inflation. In the **stock market**, optimism for lower inflation – particularly if accompanied by a higher growth outlook – may be expressed in expanding earnings multiples and rallying risk-on trades. In the **fixed income market**, lower inflation prospects should theoretically prompt lower bond yields, though securities featuring longer-dated maturities may be impacted more by other factors such as the potential for aggregate economic growth. We saw this differential play out when the FOMC cut rates by 100 basis points last year, only to have the 10-year Treasury yield *increase* by a similar amount as investors projected a more hopeful growth picture.

Thus inflation is an important component in bond yields, but it is not the only one: investors also demand compensation for holding a longer-dated security (the term premium) or choosing a riskier issuer. Bond yields are frequently the starting point for pricing loans. Typically, the longer the contract, the further out the maturity curve vehicle is used. For example, U.S. mortgages are typically tied to the 10-year U.S. T-note while Canadian mortgages are anchored by 5-year BoC debt. **This adds a layer of complexity to analysis since it's not a decision based merely on current inflation rates – it becomes a nuanced 3-D process of weighing trade-offs against future growth, credit risk and inflation.**

## How is inflation transmitted through the system?

Inflation's transmission is a lot more multi-faceted than traditional economic models are able to capture. Businesses can make choices: suspend shipments; delay M&A, R&D or expansion plans; rationalize headcount; front load purchases; seek supplier/customer concessions; change service/product composition; or raise prices. Companies usually tie many aspects of their business model to longer-term contracts, which further muddies the direct transfer of price changes.

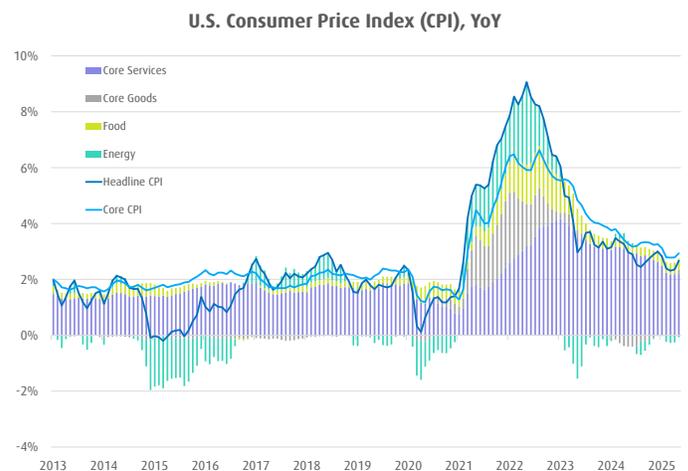
Consumers have some flexibility too. For example, they can accelerate or delay big-ticket purchases; extend time between services like haircuts, dry cleaning or lawn care; and make substitutions – house brand versus name brand, designer lipstick versus designer bag, or local park versus a week in Paris. **There are so many ways to alter the trajectory of price changes that projecting its course with any degree of confidence or accuracy is difficult.**

## Parsing the present day

As we have often noted, businesses and consumers in Canada and the U.S. have proven amazingly durable amid all the challenges lobbed at them during and after the COVID-19 pandemic. The price spikes and supply chain disruptions that occurred while the world reopened were well along in the process of being sorted out when the additional challenges of technological disruption (DeepSeek and BYD) and significantly altered political and trade policy were added to the mix earlier this year.

In the short run, investors and strategists are looking for hints that suspected inflationary aspects of the trade war(s) are being fully transmitted, though evidence has been spotty to date. The key question lurking in most minds: is inflation delayed in appearing, or will it be diverted due to other factors?

Markets seemed to interpret this week's CPI report as a hint that the transmission process was merely delayed and its conduction may be picking up steam. While the aggregate increase was largely in line with expectations, under the surface showed more dispersion. Large increases in appliance and sporting goods prices (areas already subject to tariffs) were partially offset by softness in housing costs, energy, airfares and autos. The chart below illustrates the change in key components – plus the trajectory before, during and after the "great reflation" of the pandemic era.



Canada's CPI was also released on Tuesday and showed similar under-the-hood attributes. After the releases, fixed income markets pushed longer-dated yields *higher*. In Canada, in fact, 10-year bond yields touched a level higher than when the BoC began its 225 basis point cutting campaign in 2024. Wednesday's PPI report also unexpectedly showed tame total inflation at the producer level, though softness in services spending offset noticeable upticks for hard-goods makers. Commentary from managements releasing Q2 earnings in coming weeks will definitely be worth digging into.

**It's too soon to accurately determine if tariff transmission will be one and done, or an ongoing issue.** Companies are well aware that consumers are cranky about the overall level of prices, making it a challenge to pass them on directly. To the extent manufacturers or retailers absorb the tariffs, corporate margins may suffer (though they remain at multi-decade highs so there is some room to absorb). In highlighting probable future paths, we

hesitate to put too much weight on a single month's statistics. Then, too, **the pro-growth impacts of the OBBB (see [WSP - Sketching the Second Half](#)), newly announced investments in grid enhancements, continued data-center spend and reshoring activities could well strengthen the growth outlook - but with an unknowable influence on inflation.**

Longer term, the debate still rages over what level of go-forward inflation will be normal once the disruptions of the current decade play out. **We expect the new normal will look more like the decades prior to the Global Financial Crisis when inflation and policy rates were in the low single digits versus the zero or negative rates that prevailed for much of the late aughts.**

## Implications for investors

As Ronald Reagan pointed out some 40 years ago, inflation is a tax on future growth. Unfortunately for investors, modeling and assessing inflation's run rate and ultimate impact can be difficult; so many factors conspire to move the needle up and down.

While we are waiting for the data to roll in and the various policy and growth initiatives to play out, diversification, active management and a heaping helping of patience should be an effective strategy.

## In focus in North America

Jon Borchardt, Sr. Analyst

George Trapkov, CFA, VP and Portfolio Manager

### This week

**U.S. constructive narrative pivot moves forward** – This week's Pennsylvania Energy and Innovation Summit brought together federal, state and business leaders from a wide range of disciplines sharing a common goal: position Pennsylvania as a national hub for energy and AI. President Donald Trump attended the event, which featured over \$90 billion in announced investments. Pennsylvania sits at the heart of the Appalachian Basin, home to more than 200 trillion cubic feet of recoverable natural gas – the most prolific basin in the country, accounting for roughly one-third of total U.S. production. However, growth has been constrained by environmental opposition and policy resistance to new pipeline development. Data centers – which are highly energy intensive – have been the fastest-growing segment within overall U.S. construction activity. Tech executives at the summit unveiled plans to build new facilities in Pennsylvania, aiming to capitalize on the region's low-cost stranded gas resources. Natural gas wasn't the only winner: several companies also announced investments tied to nuclear capacity expansion, and Google signed the largest-ever corporate power purchase agreement for hydropower. Utility and midstream companies committed to major grid and pipeline modernization projects. Conspicuously absent from the discussion were wind and solar as the focus shifted toward reliability over renewables. While the timelines for these projects appear ambitious, both state and federal leaders signaled a commitment to reducing regulatory hurdles in order to accelerate progress. Collectively, these announcements mark a historic pivot in U.S. energy policy.

**Canadian jobs market shows strength** – Employment surged 83,100 in June. Private sector jobs increased by 46,600 while the public sector added 23,400 spots. The unemployment rate fell slightly to 6.9%, while the participation rate rose a tick to 65.4%. Notably, employment for ages 25 to 54 rose 90,600 (the largest increase on record, excluding the 2020-to-2022 pandemic distortion). This lowered their jobless rate to 5.8%, reversing May's increase. Regionally, Alberta, Ontario and Quebec accounted for the bulk of job gains, while Atlantic Canada was a soft spot. The report numbers were significantly better than expected. It appears that the economy is hanging in there for now, pending the result of ongoing trade negotiations. This uncertainty will likely keep the BoC on the sidelines when it meets July 30.

**Canadian consumer prices remain sticky** – Consumer prices rose 0.1% in June, increasing the headline inflation rate to 1.9% from 1.7% in the prior two months. Perhaps more importantly, the two major measures of core inflation remained stubbornly stuck right around 3%; median edged up a little to 3.1% and the trim mean held fast at 3.0%. A few reasons for the sticky core inflation: only gradual receding of shelter costs; some pressures from the trade war; and higher vehicle prices. Food prices caught a little break on a large drop in veggie prices (down 1.9% year over year), but are still up nearly 3% year over year, and restaurant meals are running

a bit hotter still. Prepared food trends remain strong, with tariffs biting in a few categories here, while coffee prices have charged up 23.2% year over year, the fastest rise in almost 30 years. The inflation report gives the Bank of Canada almost nothing that would justify a rate cut in July. If the solid employment report was the icing on the cake for that decision, this is the cherry on top. Simply put, underlying inflation remains stubbornly strong. We'll need to see a material deceleration in core inflation for a cut even at the September meeting to be a possibility – barring a steep deterioration in the economy (which can't be ruled out given the ongoing tariff uncertainty).

**FOMC Chair Powell under fire again** – The Trump administration has once again escalated its pressure campaign on the Federal Reserve, seeking to influence the independent agency to aggressively cut interest rates. Equity markets declined Wednesday morning after multiple news outlets reported that President Trump had drafted a letter calling for the removal of Federal Reserve Chair Jerome Powell. The market reaction was short lived, however, after Trump told reporters he had discussed "the concept" of removing Mr. Powell with a group of congressional Republicans, but said such an outcome was "highly unlikely" unless legal justification emerges. In May, the Supreme Court ruled that the president likely holds the authority to remove officials at certain independent government agencies. However, it carved out an exception for the Federal Reserve, citing the quasi-private structure of the central bank and reaffirming that the Fed chairman cannot be removed without cause. In recent weeks, Republican lawmakers have intensified attacks on Powell, accusing him of misleading Congress about the scale of capital expenditures for the renovation of the circa-1937 Federal Reserve Board building. During testimony before the Senate Banking, Housing and Urban Affairs Committee last month, Mr. Powell rejected those claims and offered full access to documents and personnel to support congressional oversight. He has since opened the books to the inspector general for independent review. These continued attacks appear aimed at creating the conditions for a legal case to justify removal. On Wednesday, House Speaker Mike Johnson said he believed new leadership at the Fed would be "helpful." Treasury Secretary Scott Bessent confirmed that a formal search for Mr. Powell's replacement is underway. This political drama may induce greater market volatility. Ironically, it could also backfire. FOMC members may seek to reinforce the Fed's independence by resisting calls for rate cuts. Chair Powell has stated he has no intention of stepping down before his term ends next year.

**U.S. inflation tamer than expected** – There is some smoke but so far no clear signs of fire on the inflation front as investors continue to brace for U.S. tariff policy to work its way through supply chains and ultimately reach the consumer. Headline inflation readings at both the producer and consumer levels came in below Wall Street expectations, yet in both cases this was driven by weaker-than-expected inflation in the service sector, which more than offset stronger-than-anticipated goods inflation.

As we move into calendar Q2 earnings season, investor focus will turn to tariff-related margin pressures and potential impacts on consumer pricing. Forward guidance issued during Q1 earnings appeared to reflect a view that inflation fears had peaked and, until a few weeks ago, tariff risk seemed to be receding. That changed after new threats of steeper-than-expected tariffs starting August 1. The announced rate for Brazil is 50%, while Europe and Mexico were notified they face 30% duties.

This renewed uncertainty around inflation reinforces the case for the Federal Reserve to remain on hold. Dallas Fed President Lorie Logan remarked this week: "While the last several monthly inflation prints have been encouraging, short streaks of good news have raised hopes before, only to disappoint people when inflation rebounded. So, I'd like to see low inflation continue longer to be convinced."

## Next week

Earnings season gains momentum in the U.S. with mid-sized banks, a sprinkling of tech and some consumer names. A relatively sparse economic calendar though the U.S. Leading Economic Indicators on Monday and PMIs on Thursday, may generate some attention. Fixed income markets may be touchy given limited news flow from central banks in the U.S. and Canada – both have policy setting meetings the following week.

- **Monday 7/21** – U.S. Leading Economic Indicators | Canada PPI and BoC Business Outlook survey
- **Wednesday 7/23** – Canada New Housing Price Index
- **Thursday 7/24** – U.S. Initial jobless claims, Services and Manufacturing PMIs | Canada Retail and Manufacturing sales
- **Friday 7/25** – U.S. Durable-goods orders | Canada Average weekly earnings, Wholesale sales, Budget balance

## Data scorecard as of July 16, 2025

Equity Market Total Returns						
	7/16/2025 Level	WTD	YTD	2024	2023	2022
S&P 500	6,264	0.1%	7.3%	25.0%	26.3%	-18.1%
NASDAQ	20,730	0.7%	7.8%	29.6%	44.7%	-32.5%
DOW	44,255	-0.3%	5.0%	15.0%	16.2%	-6.9%
Russell 2000	2,227	-0.3%	0.6%	11.5%	16.9%	-20.5%
S&P/TSX	27,153	0.5%	11.5%	21.7%	11.8%	-5.8%
MSCI EAFE	9,487	-1.5%	17.4%	3.8%	18.2%	-14.5%
MSCI EM	672	0.9%	17.1%	7.5%	9.8%	-20.1%
Bond Market Total Returns						
		WTD	YTD	2024	2023	2022
Bloomberg U.S. Aggregate		-0.1%	3.1%	1.3%	5.5%	-13.0%
Bloomberg U.S. Treasury		-0.1%	2.8%	0.6%	4.1%	-12.5%
Bloomberg U.S. Corporate		-0.1%	3.3%	2.1%	8.5%	-15.8%
Bloomberg U.S. High Yield		-0.1%	4.5%	8.2%	13.4%	-11.2%
Bloomberg 1-10 Year Munis		-0.2%	2.0%	0.9%	4.5%	-4.7%
Bloomberg Canada Aggregate		-0.5%	-0.6%	4.0%	6.5%	-11.3%
Bloomberg Canada Treasury		-0.5%	-0.9%	2.9%	5.0%	-9.9%
Bloomberg Canada Corporate		-0.3%	1.2%	6.9%	8.2%	-9.5%
Government Bond Yields						
	7/16/2025	Last Month End	Last Quarter End	2024	2023	2022
U.S. 10-Year Treasury	4.46%	4.23%	4.23%	4.57%	3.88%	3.88%
Canada 10-Year Government	3.58%	3.27%	3.27%	3.23%	3.11%	3.30%
U.K. 10-Year Gilt	4.64%	4.49%	4.49%	4.56%	3.53%	3.66%
German 10-Year Bund	2.69%	2.61%	2.61%	2.36%	2.02%	2.57%
Japan 10-Year Government	1.58%	1.43%	1.43%	1.09%	0.61%	0.41%
Currencies & Real Assets						
	7/16/2025 Level	WTD	YTD	2024	2023	2022
USD Index	98.39	0.6%	-9.3%	7.1%	-2.1%	8.2%
CAD:USD	\$0.73	0.1%	5.1%	-7.9%	2.3%	-6.7%
Bitcoin	\$119,972.91	1.9%	28.0%	120.5%	157.0%	-64.3%
Gold	\$3,347.13	-0.3%	27.5%	27.2%	13.1%	-0.3%
Oil (WTI)	\$66.38	-3.0%	-7.4%	0.1%	-10.7%	6.7%

\*Benchmark data does not reflect actual investment performance but reflects benchmark results of the underlying indices referenced. You cannot invest directly in an index. Index definitions can be found at the end of this publication.

## Index Definitions

### Equity indices

**S&P 500® Index** is an index of large-cap U.S. equities. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

**NASDAQ Composite Index** is a market-cap weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange.

**Dow Jones Industrial Average (“DOW”)** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq.

**Russell 2000® Index** (Russell 2000®) is an unmanaged index that measures the performance of the smallest 2000 U.S. companies in the Russell 3000® Index.

**S&P/TSX Index** is a capitalization-weighted equity index that tracks the performance of the largest companies listed on Canada’s primary stock exchange, the Toronto Stock Exchange (TSX).

**MSCI EAFE Index (Developed Markets —Europe, Australasia, and Far East Index)** is a standard unmanaged foreign securities index representing major non-U.S. stock markets, as monitored by Morgan Stanley Capital International. The index captures large and mid-cap representation across 21 developed markets countries around the world, excluding the U.S. and Canada.

**MSCI Emerging Markets Index** is a market capitalization weighted index representative of the market structure of the emerging markets countries in Europe, Latin America, Africa, Middle East and Asia. Prior to January 1, 2002, the returns of the MSCI Emerging Markets Index were presented before application of withholding taxes.

### Fixed income indices

**Bloomberg U.S. Aggregate Bond Index** is an unmanaged index that covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities.

**Bloomberg U.S. Treasury Index** is an unmanaged index that includes a broad range of U.S. Treasury obligations and is considered representative of U.S. Treasury bond performance overall.

**Bloomberg U.S. Corporate Bond Index** measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

**Bloomberg U.S. Corporate High Yield Index** is an unmanaged index that covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody’s, Fitch and S&P is Ba1/BB+ or below.

**Bloomberg 1-10 Year Blend Municipal Bond Index** is a market value-weighted index which covers the short and intermediate components of the Bloomberg Capital Municipal Bond Index — an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market.

**Bloomberg Canada Aggregate Bond Index** measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market. It includes treasuries, government-related, and corporate issuers.

**Bloomberg Canada Aggregate Bond Index - Treasury** is the treasury sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.

**Bloomberg Canada Aggregate Bond Index - Corporate** is the Corporate sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.



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