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BoC Delivers a Hawkish Cut, Says Its Work is Done

- **The policy rate was cut by 25bps to 2.25%...**
- **...and guided to be at "about the right level"**
- **BoC's inflation forecasts backs up its narrative that they are done**
- **They've learned a lot about the supply side they ignored in the pandemic**
- **No changes to other policies; BoC still on track to buy T-bills this quarter**
- **Now onto next week's Budget**

The Bank of Canada cut its overnight rate by 25bps to 2.25% as widely expected. It also employed the language of central bankers to convey the message that they are done with easing unless big, negative shocks emerge. There were no shifts in balance sheet policy or related intentions. The overall signals are consistent with our forecast for the BoC to be done easing with the next move more likely to be up than down but after a lengthy pause.

Markets reacted as shown in charts 1–2. The 2s yield backed up by a handful of basis points and the 5s yield—key to the housing market—increased by around 5bps. USDCAD fell (CAD appreciated) by about a quarter of a cent. OIS markets now have the BoC on hold on December 10th and January 28th with at most about half of a quarter point cut priced around Springtime. That's likely still too much. The TSX slipped on guidance that cuts are probably done.

Overall, this is kind of a replay of 2015. Monetary policy is being fine-tuned. They are coming off the bench to add a touch more of a nudge in response to a terms of trade shock (then oil, today more about tariffs). They are not embracing a major down leg for the policy rate.

Chart 1

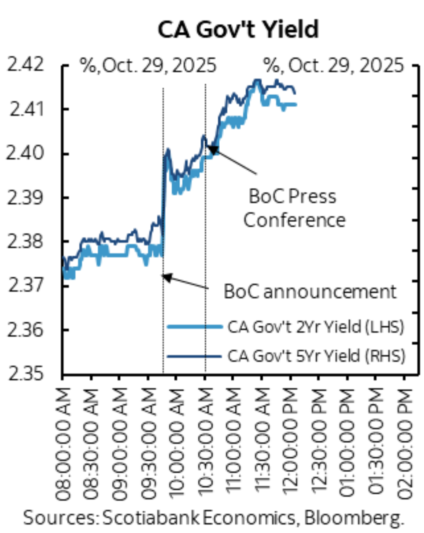


Chart 2

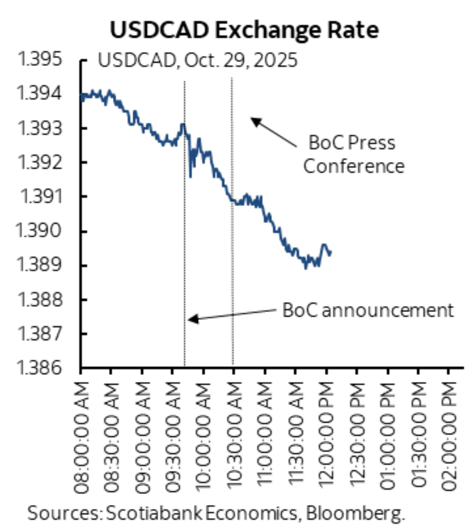


Chart 3

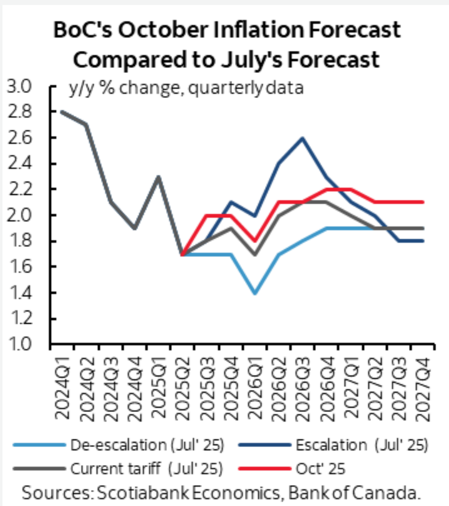
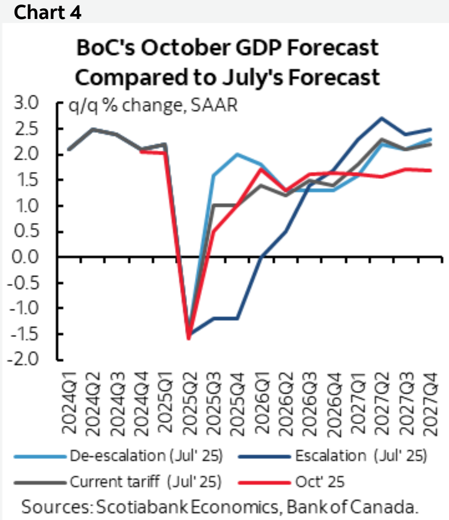


Chart 4



HAWKISH BIAS RELATIVE TO MARKETS

Key is the second last paragraph of the statement that said this with emphasis added:

> "If inflation and economic activity evolve broadly in line with the October projection, Governing Council sees ***the current policy rate at about the right level*** to keep inflation close to 2% while helping the economy through this period of structural adjustment."

UPDATED FORECASTS—DONE ENOUGH TO HIT THEIR TARGET

This statement codification of the policy bias is backed up by forecasts. Pages 54–55 of the MPR have the numbers that matter. Always save your most important points for the back pages of a hefty if not unwieldy tome I always say!

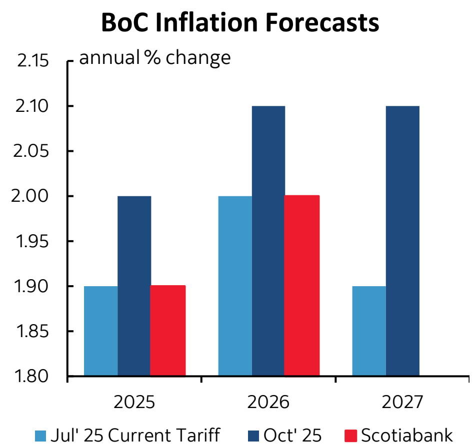
Their CPI inflation forecast is little changed (chart 3). q4/q4 2026 is now 2.2% up from 2.1%, 2027 is at 2.1%. This backs up their current assessment that they've done enough to achieve the target over the medium term. We'll see, as the BoC's ability to forecast inflation is poor, but for now I like the bias.

The BoC expects very tepid growth of 0.5% q/q SAAR in Q3, then 1.0% in Q4. That's as far out as they ever go for the quarterly projections. q4/q4 GDP growth is expected to be 1.6% in 2026 and 2027 which is somewhat weaker than previously (chart 4).

Also see the forecast comparisons in charts 5 and 6.

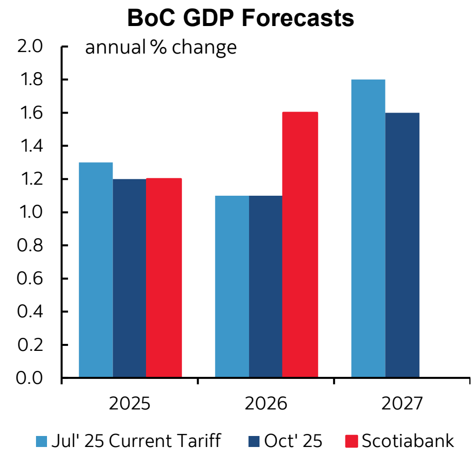
The rub lies in the fact that the GDP profile is within spitting distance of most estimates of the economy's potential rate of growth to be updated along with fresh neutral rate estimates into the April 2026 MPR. They project that slack will stop rising. They are also signalling that significant capacity is being destroyed by the US-driven trade war.

Chart 5



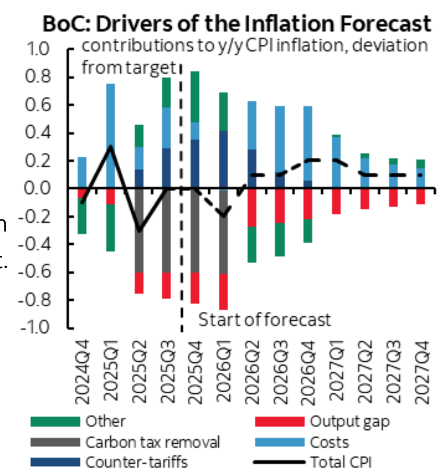
Sources: Scotiabank Economics, Bank of Canada *Monetary Policy Report - Oct 2025.*

Chart 6



Sources: Scotiabank Economics, Bank of Canada *Monetary Policy Report - Oct 2025.*

Chart 7



Sources: Scotiabank Economics, Bank of Canada.

BOC EMBRACES THE SUPPLY SIDE'S LIMITS

Further to this last point, and to the BoC's credit, I find it heartening that they've learned much more about the supply side from their disastrous experience of the pandemic. They continue to strengthen the narrative that trade tensions add costs and price pressures. The statement codification of such in the final paragraph makes that clear. Largely gone is the version of Macklem in the pandemic who dismissed any inflation risk with talk of fully inclusive maximum employment. There is a wholesale reworking of the BoC's framework of thinking and modelling that allowed inflation to get out of control in the pandemic.

That's evident in chart 7 that we've recreated from the MPR and that offers the BoC's expected decomposition of the drivers of its inflation forecasts. Many on the street only look at slack (ie: output gaps). Basically, as 2026–27 unfolds, they expect slack to be offset by costs as a driver of inflation risk. 2020–22, 'costs' wouldn't have even been on there.

Recall that the next estimates for potential GDP growth and the neutral rate range will be assessed by April.

OVER TO YOU PRIME MINISTER CARNEY

The BoC faithfully stood by its practice of not saying anything about the upcoming federal budget next Tuesday while repeating they will incorporate its effects afterward. Assuming the Budget passes—which it may not—this means formally incorporating the Budget's effects in the next MPR projections in January but opining on its general effects in other communications including the December press conference. Here is their formal comment:

"The projection for government spending is based on information from published provincial budgets and new federal fiscal measures that have been tabled at the time of writing. Government spending is assumed to grow at a moderate pace in 2026 and 2027. However, the path of federal government spending will be clearer after the budget is released on November 4."

There is also the usual counter. Whatever they say publicly and flag as having been incorporated in today's forecasts, Governing Council's judgement may very reasonably be factoring in expectations for material fiscal stimulus and therefore passing the torch to Carney as part of the rational for signalling an end to rate cuts.

STEADY AS SHE GOES ON THE BALANCE SHEET

There was nothing new offered on CORRA, funding markets, or the balance sheet. I didn't expect it as I think most didn't expect anything, so it largely just reaffirms that they're pleased to see CORRA tightening over the overnight policy rate.

October 29, 2025

That's not the same as saying the balance sheet will be boring in future. They ended QT in January but what lies ahead will be key. 2026 will liven up the debate over gross Government of Canada bond purchases in the normal conduct of monetary policy (ie: not QE). They're still quite some distance away from that, but the dialogue will emerge more significantly as the year unfolds. A hint would be the minute you see a Gravelle speech on b/s inserted. When asked in the press conference, SDG Rogers said that they still plan on buying T-bills this quarter as per prior plans. She went no further.

HIKE NEXT?

A 2.25% o/n rate lies at the bottom end of the neutral rate range. It's basically zero in real terms. That's not long-run equilibrium stuff especially given that cost and price pressures are at a highly nascent stage of developments that are pointed upward over time. I've argued for a while now that 5s are likely rich. At present there is little term premia and eventually we start to get into a steeper belly in anticipation of unwinding these cuts and maybe going further than that. This view is supported by a long wave narrative on cost and price pressures globally especially in Canada, plus cautious optimism in our projections that the economy gains some momentum later in our projection period as it adjusts to the tariff shock, while monetary easing works through alongside fiscal easing and CAD continues to be a shock absorber.

STATEMENT COMPARISON AND LINKS

Please see the last page for a comparison of this statement and the one in September. Key is the changed guidance.

Go **here** for the BoC's statement, **here** for the MPR, **here** for Governor Macklem's opening remarks.

PRESS CONFERENCE TRANSCRIPT

What follows is my attempt at providing a transcript of the Q&A banter during the press conference. Any errors or omissions are to be blamed on my typing fingers.

Q1. The policy rate is only at the lower end of the neutral range but your projection is weak. You speak about constraints around monetary policy. Why are we not talking about more easing?

A1. We're now at the lower end of our neutral rate range so monetary policy is stimulating. The role of monetary policy is somewhat limited. We are not in just a cyclical downturn. Part of it is. Demand for products in the US is lower which is partly cyclical. But part of it is structural. The US has swerved to protectionism. That has destroyed some productive capacity in this economy. It adds costs as businesses are configuring supply chains. The fact it is adding costs limits the role of monetary policy in boosting demand while keeping inflation low. Monetary policy can't target specific sectors that are targeted. It can't help companies find new markets or reconfigure supply chains. It can try to mitigate the spillover effects into other parts of the economy but it's role is limited. This is more than a cyclical downturn. There are structural challenges that limit our flexibility.

Q2. Are you signalling you are done today? Is it now up to fiscal authorities to help adjustments? Is there anything fiscal policy should deliver next week?

A2. There is a lot of uncertainty and a wider than usual range of outcomes relative to the outlook. We'll be assessing relative to our outlook. If the outlook changes materially then yes we are prepared to respond. But our message is with this cut today and if the outlook evolves as expected then we think the current policy rate is about where it should be. We're going to get the Budget next week so let's just wait for that. We'll take on board what is done in our projections. [ed. they won't do that formally until the Jan MPR...]

Q3. You mention CAD as an upside to inflation risk. Is CAD reacting more permanently as a shock absorber?

A3. Rogers responding. CAD is responding as a shock absorber. Soem correlations with drivers are a bit less tight than historically. CAD is responding the way it usually does.

Q4. The MPR expects slower consumption growth in the next two years. Why will it fade when it has been holding up?

A4. We don't have a lot of growth in the forecast but we do have growth and it's really consumption that is underpinning that. Growth is very weak in the near term because of exports and investment and then you start to see it pick up as exports and investment start to recover. What is underpinning this is further easing. We don't think consumption will stay as strong as it was in Q2 as population growth is low in the forecast and confidence and uncertainty weigh on spending. [ed. should've answered 'services!'. ie: the nontradeable sector which remains very buoyant even now].

Q5. General question on trade and advice to job seekers

A5. The economy will be less efficient and growth will be lower. There are things that can bend the growth path upward but they are not what monetary policy can do. We need to get productivity growth up. Unless we change those other things then our standard of living will be permanently lower.

Q6. What could alter your outlook?

A6. You need to see sustained developments that are material and we are prepared to respond if we see that. With this cut based on this outlook we think the current policy rate is about right.

Q7. Was the intent to signal that the policy rate is at the right level because of upside risks to inflation as fuelled by tariffs and the change in the global backdrop?

A7. Above all our job is to maintain low inflation. There is a role for monetary policy to play in helping the economy adjust but we can't lose sight of our inflation objective.

Q8. Would a further investment in AI offset the hit from US tariffs?

A8. AI does have great potential to improve productivity to raise standard of living. AI has the potential to create new products but also disrupt. The most recent Nobel Prize in economics is about just that. The process of innovation can create opportunities and destroy others. It is unclear exactly how transformative AI is. What the balance is between long-term gain and disruption. Our sense is this will play out faster than previous technology shocks.

Q9. DepGov Gravelle said the BoC will restart t-bill buying in Q4. Is that still the same or does it depend on the budget?

A9. Our plan hasn't changed. If it changes, we would provide advance notice. Everything remains on track. [ed. too bad the question didn't go further about what's next in 2026….tbc].

Q10. Comments on financial stability? Is it a good bubble or bad one in US stocks?

A10. In the risks section of the MPR we did highly one of the risks being stretched equity valuations. The AI boom is in full flight. If there were a shift in sentiment about the payoff of AI you could see a sharp revaluation downward. Yes that could have some economic consequences.

Q11. Do your models indicate whether a 25bps cut is enough to offset the trade shock and population weakness on housing?

A11. Rogers answering. We don't specifically model the impact on housing. Speaking generally about affordability differences by region. It's a really diverse housing market with more acute challenges in Toronto condos. We do see some pick up in housing activity in the forecast.

Q12. Does the BoC still think Canada will avoid a recession in 2025? Where is growth coming from in 2026?

A12. Q2 GDP was negative. Our outlook has growth resuming in H2 to be very modest. When we forecast a small positive we can't rule out a small negative. We can't rule out a couple of negative quarters. What I would emphasize is they're not going to feel good. We're not forecasting a sharp down draft in the Canadian economy with a big rise in the unemployment rate more typical of past recessions. What is supporting growth? Consumption and housing have been pretty resilient. We think consumption growth will moderate. By lowering interest rates we are providing more support. Government spending is also contributing to growth. What's weak in the near-term is exports and business investment. Coming into next year they start to recover. With that GDP picks up in 2026-27.

RELEASE DATE: OCTOBER 29, 2025

The Bank of Canada today reduced its target for the overnight rate by 25 basis points to 2.25%, with the Bank Rate at 2.5% and the deposit rate at 2.20%.

With the effects of US trade actions on economic growth and inflation somewhat clearer, ***the Bank has returned to its usual practice of providing a projection for the global and Canadian economies*** in this *Monetary Policy Report* (MPR). Because US trade policy remains unpredictable and uncertainty is still higher than normal, this projection is subject to a wider-than-usual range of risks.

While the global economy has been resilient to the historic rise in US tariffs, the impact is becoming more evident. Trade relationships are being reconfigured and ongoing trade tensions are dampening investment in many countries. In the MPR projection, the global economy slows from about 3¼% in 2025 to about 3% in 2026 and 2027.

In the United States, economic activity has been strong, supported by the boom in AI investment. At the same time, employment growth has slowed and tariffs have started to push up consumer prices. Growth in the euro area is decelerating due to weaker exports and slowing domestic demand. In China, lower exports to the United States have been offset by higher exports to other countries, but business investment has weakened. Global financial conditions have eased further since July and oil prices have been fairly stable. The Canadian dollar has depreciated slightly against the US dollar.

Canada's economy contracted by 1.6% in the second quarter, reflecting a drop in exports and weak business investment amid heightened uncertainty. Meanwhile, household spending grew at a healthy pace. US trade actions and related uncertainty are having severe effects on targeted sectors including autos, steel, aluminum, and lumber. As a result, GDP growth is expected to be weak in the second half of the year. Growth will get some support from rising consumer and government spending and residential investment, and then pick up gradually as exports and business investment begin to recover.

Canada's labour market remains soft. Employment gains in September followed two months of sizeable losses. Job losses continue to build in trade-sensitive sectors and hiring has been weak across the economy. The unemployment rate remained at 7.1% in September and wage growth has slowed. Slower population growth means fewer new jobs are needed to keep the employment rate steady.

The Bank projects GDP will grow by 1.2% in 2025, 1.1% in 2026 and 1.6% in 2027. On a quarterly basis, growth strengthens in 2026 after a weak second half of this year. Excess capacity in the economy is expected to persist and be taken up gradually.

CPI inflation was 2.4% in September, slightly higher than the Bank had anticipated. Inflation excluding taxes was 2.9%. The Bank's preferred measures of core inflation have been sticky around 3%. Expanding the range of indicators to include alternative measures of core inflation and the distribution of price changes among CPI components suggests underlying inflation remains around 2½%. The Bank expects inflationary pressures to ease in the months ahead and CPI inflation to remain near 2% over the projection horizon.

With ongoing weakness in the economy and inflation expected to remain close to the 2% target, Governing Council decided to cut the policy rate by 25 basis points. ***If inflation and economic activity evolve broadly in line with the October projection, Governing Council sees the current policy rate at about the right level to keep inflation close to 2% while helping the economy through this period of structural adjustment. If the outlook changes, we are prepared to respond.*** Governing Council will be assessing incoming data carefully relative to the Bank's forecast.

The Canadian economy faces a difficult transition. The structural damage caused by the trade conflict reduces the capacity of the economy and adds costs. This limits the role that monetary policy can play to boost demand while maintaining low inflation. The Bank is focused on ensuring that Canadians continue to have confidence in price stability through this period of global upheaval.

RELEASE DATE: SEPTEMBER 17, 2025

The Bank of Canada today reduced its target for the overnight rate by 25 basis points to 2.5%, with the Bank Rate at 2.75% and the deposit rate at 2.45%.

After remaining resilient to sharply higher US tariffs and ongoing uncertainty, global economic growth is showing signs of slowing. In the United States, business investment has been strong but consumers are cautious and employment gains have slowed. US inflation has picked up in recent months as businesses appear to be passing on some tariff costs to consumer prices. Growth in the euro area has moderated as US tariffs affect trade. China's economy held up in the first half of the year but growth appears to be softening as investment weakens. Global oil prices are close to their levels assumed in the July Monetary Policy Report (MPR). Financial conditions have eased further, with higher equity prices and lower bond yields. Canada's exchange rate has been stable relative to the US dollar.

Canada's GDP declined by about 1½% in the second quarter, as expected, with tariffs and trade uncertainty weighing heavily on economic activity. Exports fell by 27% in the second quarter, a sharp reversal from first-quarter gains when companies were rushing orders to get ahead of tariffs. Business investment also declined in the second quarter. Consumption and housing activity both grew at a healthy pace. In the months ahead, slow population growth and the weakness in the labour market will likely weigh on household spending.

Employment has declined in the past two months since the Bank's July MPR was published. Job losses have largely been concentrated in trade-sensitive sectors, while employment growth in the rest of the economy has slowed, reflecting weak hiring intentions. The unemployment rate has moved up since March, hitting 7.1% in August, and wage growth has continued to ease.

CPI inflation was 1.9% in August, the same as at the time of the July MPR. Excluding taxes, inflation was 2.4%. Preferred measures of core inflation have been around 3% in recent months, but on a monthly basis the upward momentum seen earlier this year has dissipated. A broader range of indicators, including alternative measures of core inflation and the distribution of price changes across CPI components, continue to suggest underlying inflation is running around 2½%. The federal government's recent decision to remove most retaliatory tariffs on imported goods from the US will mean less upward pressure on the prices of these goods going forward.

With a weaker economy and less upside risk to inflation, Governing Council judged that a reduction in the policy rate was appropriate to better balance the risks. Looking ahead, the disruptive effects of shifts in trade will continue to add costs even as they weigh on economic activity. ***Governing Council is proceeding carefully, with particular attention to the risks and uncertainties.*** Governing Council will be assessing how exports evolve in the face of US tariffs and changing trade relationships; how much this spills over into business investment, employment, and household spending; how the cost effects of trade disruptions and reconfigured supply chains are passed on to consumer prices; and how inflation expectations evolve.

The Bank is focused on ensuring that Canadians continue to have confidence in price stability through this period of global upheaval. We will support economic growth while ensuring inflation remains well controlled.

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