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GLOBAL ECONOMICS

SCOTIA FLASH

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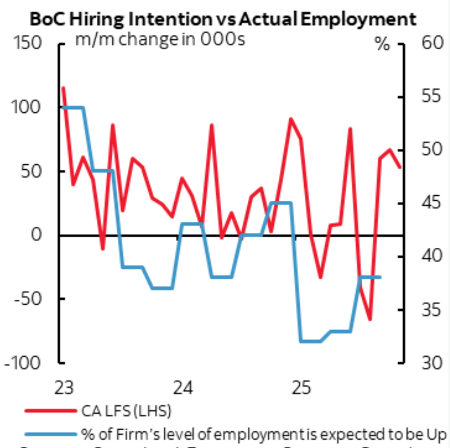
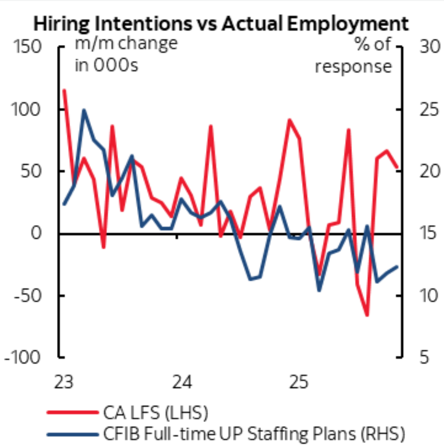
Chart 1



Sources: Scotiabank Economics, Statistics Canada, Bank of Canada.

Chart 2



Sources: Scotiabank Economics, Statistics Canada, CFIB.

BoC Puts on Horse Blinders for the Holidays

- **BoC held the policy rate at 2¼% as universally expected**
- **Forward guidance continued to point to a long hold**
- **The script broadly met expectations not to rock the boat…**
- **…but the street should challenge the BoC's fading of recent developments**
- **Macklem dodged a golden opportunity to lean against hike pricing**
- **Canadian & US rates rallying roughly in tandem, CAD firmer, FOMC up next**

The Bank of Canada kept its policy rate unchanged at 2.25% as universally expected and left guidance intact that it is on a prolonged hold while emphasizing uncertainty. That shouldn't have surprised anyone in a don't-rock-the-boat before the holiday season sense and with the long gap before the next decision seven weeks from now.

That's not the same as saying their stance is beyond reproach. The BoC conveniently looked through most of the key developments and I'll return to explaining this after recapping what they said. For now, the short and cautious message drove some positioning covering in the Canadian rates curve and a small decline in yields that consolidates only a modest portion of the rate hike pricing for later next year.

UNCHANGED LONG PAUSE GUIDANCE

Forward rate guidance was left unchanged as follows

"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."

To which they added "Uncertainty remains elevated." Indeed. That's new in that part of the statement, but not new elsewhere in the statement as they emphasized that "uncertainty is still higher than normal" in the prior statement.

A VERY SHORT STATEMENT

Please see the appendix for a comparison of today's statement and the October version. What should jump out is the brevity. It's just over half the length. Part of that is because this was a non-MPR meeting. Part of it is because they don't want to rock the boat.

I'll go over some of the key takeaways from the statement next.

HERE COME THE YEAH, BUTS

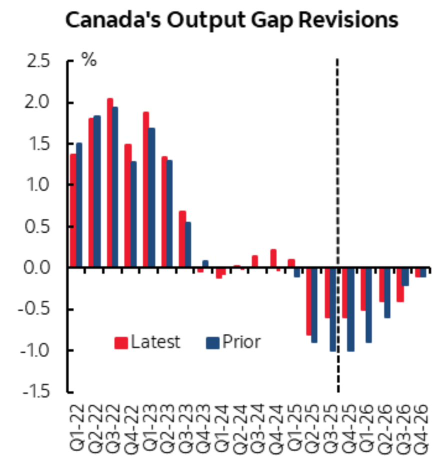
My overall takeaway here is that the BoC bought time until it does a proper job at the end of January with more information. For now, they put on horse blinders and heavily faded developments in ways I think went too far. There are three main examples.

Jobs ripping? Yeah but look at the soft hiring intentions data was the message here. The counter to this stance from the BoC is that intentions data is largely useless as a guide to actual hiring decision so why emphasize it? Doing so is a vain attempt at ignoring the fact the job markets has blown away their expectations—and everyone else's. Charts 1–2 show the BoC's business survey measure of hiring intentions that has been bleak all year and the CFIB's small business measure of hiring intentions that has been bleak since last year, versus the often high and generally robust trend in hiring figures.

GDP revisions and impacts on slack? Yeah but we don't have any numbers for you now [of course they do] but we're told they "roughly" balance out in supply and demand implications for the amount of slack. Define 'roughly' is my counter. We think the new data cut the estimated amount of slack in the economy 'roughly' in half as at Q3 compared to previously and did so by looking at the same set of numbers the BoC does (chart 3). From –1.1% to around –0.6% or so is reasonable. If the BoC is going to fade all of that by staying at –1.1% then I'd like to see their math while bearing in mind that they've (in my opinion) invoked some pretty arbitrary assumptions on potential GDP and hence the supply side in the past.

What about the fiscal policy effects on the outlook? Dunno, haven't really estimated that, but there are supply and demand effects from the federal budget. Of course they've looked at the effects. But just wait until the next forecasts before the BoC unveils the estimated impact as they see it.

Chart 3



Source: Scotiabank Economics.

SO WHY'D THEY DO IT?

There are several possible reasons. One is that it's somewhat prudent not to overreact to recent developments, and one example is that it's highly unlikely that the job growth trend of the past three months is sustainable at such rates although it's unclear if it just slows or sustainably craters.

On the flip side, I also worry about a central bank that fades or undermines them.

Two is that there are many uncertainties going forward and it's premature to rock the boat. That's not the same as saying that the *street* shouldn't rock the boat on these developments. And uncertainties can turn out better or worse as opposed to viewing them as meaning only bad outcomes. CUSMA, for instance, could go off the rails. Or the pattern to date to respect it outside of steel and aluminum and parts of autos (ie: most of the economy that is not in those sectors) could be a sign of action versus rhetoric in Washington. Tear it up into midterm when you're already polling poorly? I'll take the other side of that one.

In all, this was the expected denial report. Don't rock the boat, see you in seven weeks when we have full forecasts and some actual data on what's going on in the US. But don't be lulled into putting on horse blinders yourselves.

MACKLEM PASSED ON AN OPPORTUNITY TO FADE HIKE PRICING

And yet, Governor Macklem was given a golden opportunity to lean against market pricing for rate hikes as soon as late next summer into Fall and he passed. Totally whiffed. Ninth inning, bases loaded, winning run at the plate, and whoooof.

See the exchange in Q#4 of the press conference recapped below. Macklem could be reasonably expected not to lean one way or the other that far out amidst the uncertainty. But if he had a strong opinion and wanted to control the path forward then he could have done so with a word or two and he did not.

He also noted that "so far, the economy is proving resilient overall" which is the same messaging you are hearing from the ECB, BoJ, Fed, and Antipodeans. These central bankers are herd bound and generally tend to move together.

PRESS CONFERENCE RECAP

What follows is an attempt at a recap of the Q&A portion of the press conference after Macklem was done reading his opening remarks. Any omissions or errors and to be blamed on my typing but I think it's broadly representative of the discussion. A full official transcript would be helpful!

Q1. You are downplaying three strong job markets. How are you thinking about them?

10:42:35 A1. Hiring in services has been resilient. Overall employment has moved up. That is encouraging. There is some resilience in the economy. Looking forward, it hasn't fundamentally changed our view. The Canadian economy is going through a structural adjustment. Companies are cautious about their investment and hiring plans. Going forward we continue to expect fairly modest growth.

Q2. What is the source of this resilience?

A2. It's hard to give a super precise answer. We got revisions to 2022, 2023, 2024 that showed stronger consumption and investment and productivity growth was still weak but went from zero to about 0.5. Both demand and supply were stronger. The economy was stronger than expected and that may explain some of the resilience in the data. Secondly, there are steep tariffs on some sectors like steel, aluminum, but outside of those sectors if you are compliant with those sectors then Canada's average US tariff rate is one of the lowest in the world. We haven't seen big spillovers to the rest of the economy.

December 10, 2025

Q3. How did the federal budget and provincial updates impact your outlook?

A3. What you see in the budget is increases in government spending particularly on defence that will support demand. Targeted measures including those announced before the budget will support hard hit sectors to help them pivot to other exports and domestic sources of demand. There is also a lot of focus on investment. We're still working through the macroeconomic implications. It will take some time for the macroeconomic impact to show up in the economy. That will build up over time but it's not like there is a big hit right away. The impacts will depend importantly on the speed and success of execution and how the private reacts and we'll have to come up with some forecasts for these things. The budget will add demand and supply and is not adding a lot of additional inflationary pressures.

Q4. Are traders getting ahead of pricing hikes next year?

A4. I'm going to let traders decide what to price. We've been very clear. Given how we see things right now, we think the policy rate is about right. At the lower end of the neutral range it is providing a bit of support to help the economy work through. That's how we see things now. How we see things going forward is a more difficult question and I'm not going to put our policy on a timeline. Markets can expect our decisions on a meeting by meeting basis and as conditions evolve we will update our communications. We'll be assessing developments in relation to our outlook. If developments move in one way or the other to that outlook then we are prepared to respond.

Q5. In reference to data lags and US shutdowns, if you're not getting a full picture of growth until after the fact then how does this impact your ability to conduct policy?

A5. There are a number of important bits of data Statcan gets from the US like trade. With the shutdown, the data on exports is not as good as normal [ed nor imports] but yes in the fullness of time there is a prospect of larger than normal revisions when the data comes in.

Q6. The BoC speaks about inflation returning to target but Canadians focus on costs and prices. What do you say to Canadians about affordability?

A6. Generic political answer acknowledging many Canadians are impacted by affordability but it emphasizes the important of keeping inflation low so incomes can catch up. The other thing I would stress is we're not trying to push overall prices down as that would cause a recession.

Q7. Do you think there is less slack than you anticipated in October and do you see the output gap narrowing over your projection period?

A7. We don't have a new projection. The recent data is showing some improvement and that is welcome news. That has not changed our view the economy is still in excess supply and we continue to expect modest growth going forward. New revisions for the last 3 years showed GDP quite a bit higher because of both demand (consumption) and supply (investment) drivers. I would not interpret higher GDP as purely a signal of higher demand, there are both supply and demand drivers. Before we get to January MPR we'll have to evaluate more fully. Secondly, Q3 GDP was a lot stronger than expected which mechanically would narrow slack, but the details don't look like demand was stronger as final domestic demand was slack. We expect Q4 FDD to pick up while trade weakens. The resilience we're seeing in the economy has been welcome news but it hasn't changed our views because there is still excess supply and growth is still modest.

Q8. How may tariff shocks and threats influence you next year?

A8. Through spring and summer people were talking recession and we published scenarios in the mPR that could have pushed the economy into recession. The 'r' word people are talking about now is resilience. We're ending the year in a better place than it looked in the middle of the year. But there is still a significant adjustment to work through. We're going to be assessing the impact of the budget and new data in the next MPR.

Q9. You had estimated the TMX pipeline would add 0.25% to the economy. What could be the impact of another new pipeline?

A9. I'm not going to comment on the impact at this point. We do need to diversify our trade. The TMX pipeline has been an important example that has allowed us to increase our exports to non-US markets. It's not a huge shift but on the margin it's helping us get more oil to other countries. It's also helping us getting more value out of what we export because it has narrowed the WTI-WCS spread.

Q10. Are we many months away from the need to adjust the policy rate higher?

A10. I don't have much more to add. We think the policy rate is in the right place right now.

Q11. In 2024 you said Canadians can breathe a sigh of relief that inflation has come down. There is still high uncertainty and affordability concerns. What's your message into 2025?

A11. There is a feeling of uneasiness or uncertainty overhanging Canadians right now. Our focus is inflation to provide stability to an uncertain picture.

Q12. Is it the Bank's probability to warn people of the material probability of rates going up to ward off what's happened in the past on mortgage patterns?

A12. Our responsibility is to discuss the outlook and probabilities. We put that out because monetary policy has to be forward looking. We're going to be assessing that data in relation to our outlook. If you see the data before us then you know before we adjust that our views are likely to evolve. It's our job to be really clear about where we see the economy going and it's the job of mortgage advisers etc to advise clients.

Q13. Where do you see shelter costs and the final wave of mortgage renewals going?

A13. Overall activity looks better balanced but there are many regional markets. We don't expect another surge in house prices. We expect a continued correction in some higher priced markets. Both interest rates and supply conditions are helping to improve affordability but there is a structural issue on the supply side.

RELEASE DATE: DECEMBER 10, 2025

The Bank of Canada today held its target for the overnight rate at 2.25%, with the Bank Rate at 2.5% and the deposit rate at 2.20%.

Major economies around the world continue to show resilience to US trade protectionism, but uncertainty is still high. In the United States, economic growth is being supported by strong consumption and a surge in AI investment. The US government shutdown caused volatility in quarterly growth and delayed the release of some key economic data. Tariffs are causing some upward pressure on US inflation. In the euro area, economic growth has been stronger than expected, with the services sector showing particular resilience. In China, soft domestic demand, including more weakness in the housing market, is weighing on growth. Global financial conditions, oil prices, and the Canadian dollar are all roughly unchanged since the Bank's October Monetary Policy Report (MPR).

Canada's economy grew by a surprisingly strong 2.6% in the third quarter, even as final domestic demand was flat. The increase in GDP largely reflected volatility in trade. The Bank expects final domestic demand will grow in the fourth quarter, but with an anticipated decline in net exports, GDP will likely be weak. Growth is forecast to pick up in 2026, although uncertainty remains high and large swings in trade may continue to cause quarterly volatility.

Canada's labour market is showing some signs of improvement. Employment has shown solid gains in the past three months and the unemployment rate declined to 6.5% in November. Nevertheless, job markets in trade-sensitive sectors remain weak and economy-wide hiring intentions continue to be subdued.

CPI inflation slowed to 2.2% in October, as gasoline prices fell and food prices rose more slowly. CPI inflation has been close to the 2% target for more than a year, while measures of core inflation remain in the range of 2½% to 3%. The Bank assesses that underlying inflation is still around 2½%. In the near term, CPI inflation is likely to be higher due to the effects of last year's GST/HST holiday on the prices of some goods and services. Looking through this choppiness, the Bank expects ongoing economic slack to roughly offset cost pressures associated with the reconfiguration of trade, keeping CPI inflation close to the 2% target.

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. Uncertainty remains elevated. If the outlook changes, we are prepared to respond. The Bank is focused on ensuring that Canadians continue to have confidence in price stability through this period of global upheaval.

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.