Scotiabank

GLOBAL ECONOMICS

SCOTIA FLASH

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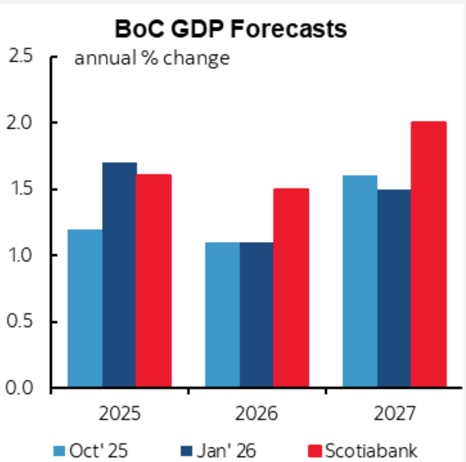
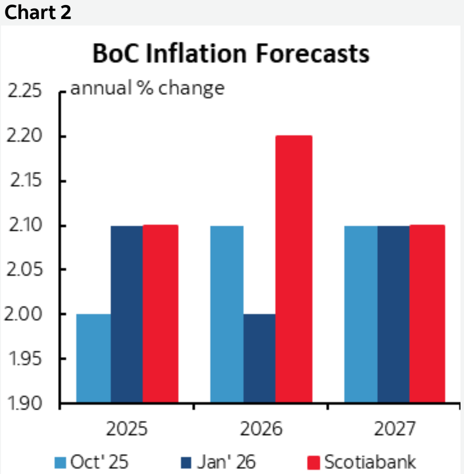
Chart 1



Sources: Scotiabank Economics, Bank of Canada *Monetary Policy Report - Jan 2026.*

Chart 2



Sources: Scotiabank Economics, Bank of Canada *Monetary Policy Report - Jan 2026.*

The BoC Met Expectations, Even if it Fudged Things

- **The policy rate was left unchanged at 2.25% as universally expected**
- **There were no changes to balance sheet or funding instruments as expected**
- **Forecast changes were minor**
- **There were multiple oddities in the overall package of views**
- **Key was ambivalence toward the direction and timing of a rate move**
- **Markets largely ignored it all**

The BoC kept its overnight rate unchanged at 2.25% as universally expected. Forward guidance was left broadly intact alongside minor forecast changes. There were no other policy changes affecting balance sheet or funding tools and none were expected.

Basically they're repeating long hold guidance until some new information arrives in either direction, while not signalling any appetite for deviating from 2.25% any time soon which is as expected. The most useful thing that was said was the response to question #10 in the press conference when Macklem was strikingly direct—and honest—in saying they weren't at all sure in what direction or when the policy rate may be changed next. While headlines emphasize the BoC's emphasis upon uncertainty, they fail to note that the BoC is speaking of bidirectional uncertainty in terms of what it means to growth and inflation and hence the policy rate. This reinforces our view for a hold through 2026H1 until things get more interesting and we have further information.

Having said that, I'll explain how I felt that the overall tone of the communications had the feel of forcing arguments to merit leaving the inflation outlook unchanged rather than raising it a touch

CAD depreciated a touch, but so did other currencies against the USD and CAD continues to slightly outperform the rest of them this morning. The Canadian two-year yield is flat compared to pre-communications. Markets continue to price the BoC on hold until about half of a 25bps hike is priced by late year. Our forecast remains for two hikes starting in October and December.

The statement is **here** and see the comparison of changes in the appendix to this note. The MPR and forecasts is **here**. Governor Macklem's remarks are **here**. I also provide an attempt at a press conference transcript.

STATEMENT CHANGES

Key is that the concluding forward guidance was similar to the last statement in December. They now say:

"Governing Council judges the current policy rate remains appropriate, conditional on the economy evolving broadly in line with the outlook we published today. "

Versus in December:

"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 references were slightly upgraded, but that could merely reflect the passage of time as January is closer to Summertime trade negotiations, US midterms, US Court rulings on tariffs and the Fed, the Fed Chair appointment etc than October was. Here's the change:

October: "Uncertainty remains elevated."

January: "Uncertainty is heightened and we are monitoring risks closely."

I remain cautiously optimistic on how the negotiations turn out.

FORECAST CHANGES AND CURIOUSITIES

Canadian GDP growth was left intact at 1.1% in 2026 and little changed for 2027 at 1.5% (1.6% previously). Chart 1.

Externally, they upped their US growth forecasts from 2.1% to 2.2% for last year with Q4 GDP still pending, from 2.2% to 2.6% for 2026, and unchanged at 2.1% for 2027. They also revised up the Euro Area, China, and World GDP figures for 2025–26.

That's all good for a trading nation, so how come they didn't revise up Canadian GDP growth as well? They basically shrug their shoulders on the direction of trade risks but fade the more positive imported effects of stronger external growth?? That sounds like an imposed bias that was left unexplained and nobody asked why.

CPI inflation is projected to be 2.0% in 2026 (2.1% previously) and 2.1% in 2027 which is unchanged from October. Chart 2. I'll come back to debatable ingredients to their views on inflation that upgraded 2025 but slightly lowered 2026 inflation.

The verbiage emphasizes little change by stating "The Bank projects growth of 1.1% in 2026 and 1.5% in 2027, broadly in line with the October projection" and "Inflation was 2.1% in 2025 and the Bank expects inflation to stay close to the 2% target over the projection period, with trade-related cost pressures offset by excess supply."

Chart 3

Canadian Core CPI Measures

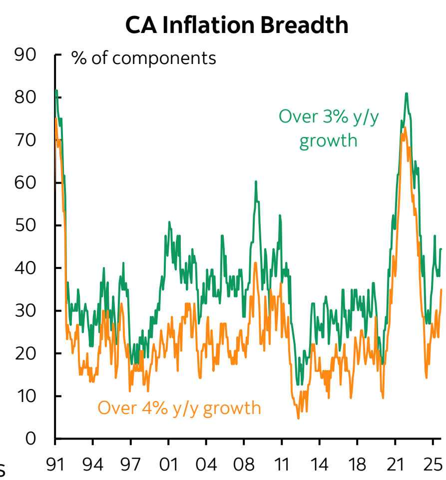
Month	Weighted Median	Trimmed Mean	Traditional Core
Jan-2025	2.8	3.4	3.2
Feb-2025	3.9	3.4	5.6
Mar-2025	1.7	2.3	0.0
Apr-2025	5.1	4.6	4.0
May-2025	2.2	2.3	3.2
Jun-2025	2.8	2.8	2.4
July-2025	1.7	2.3	0.8
Aug-2025	3.3	2.8	1.6
Sep-2025	2.8	2.8	3.1
Oct-2025	2.2	2.8	2.3
Nov-2025	1.6	1.7	1.5
Dec-2025	0.5	1.1	3.1

Sources: Scotiabank Economics, Statistics Canada.

One thing that bothers me about their inflation view is that they cherry-picked the core measures. Chart 7 in their MPR shows that the trimmed mean and weighted median measures of core inflation have eased of late. What was omitted was traditional core (ex-food and energy) that has accelerated of late (chart 3). They have at times indicated a tendency to downplay trimmed mean and weighted median CPI, but when it suits them, they play it up. Again, that's another bias.

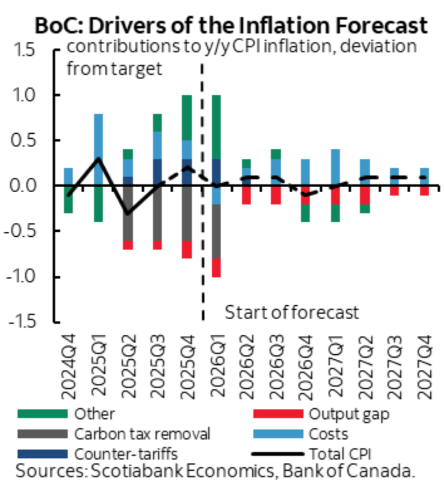
For that matter, do a keyword search for 'breadth' of inflationary pressures and you won't find a single reference in the entire MPR. Not one. Yet look at chart 4 that clearly shows a pick up. Again, their bias is may be clouding their objectivity and that's never good for a central bank.

Chart 4



Sources: Scotiabank Economics, Statistics Canada.

Chart 5



Sources: Scotiabank Economics, Bank of Canada.

They played with potential GDP in ways we contest. This year's potential range is up a bit from a range of 0.4–1.4% in October to 0.6–1.6% now but it's unclear why, but they took that back and then some by downgrading 2027 potential GDP growth to 0.7–1.7% from 1.3–2.3%. I have always found that the BoC fudges potential and gaps to suit themselves on the current bias.

Yet downgrading potential in 2027 while leaving actual GDP projections little changed should have the BoC raising its inflation projection in 2027 through less downward influence from slack. Why didn't they? I mean, we all know that forecasting that far out has umpteen uncertainties, but why don't the numbers hang together in an internally consistent fashion? My hunch is that internal consistency would have meant raising the 2027 inflation forecast and thus signalling to markets more concern about upside than downside risk which they're not yet prepared to do. BoC forecasts are notorious for reflecting what they wish to show.

They left their estimate of the output gap as at the end of 2025 unchanged in a range from -1.5% to -0.5%. ""Potential output has thus been revised up by almost as much as GDP, so the amount of slack in the economy remains largely unchanged." Here too, why? Our group estimates less slack as a result of the GDP revisions by putting a little more weight on the actual GDP revisions than the potential GDP revisions. This reflects our dissection of the underlying causes of the GDP revisions including more investment and how it works through modelling attempts. The BoC doesn't explain why they raised potential enough to offset higher GDP levels. Frankly, something smells like the foot of the Don River in summertime here.

Chart 5 is replicated from the MPR and shows a very slight tilt toward cost pressures on CPI offsetting downward effects of modest slack relative to their previous breakdown in October.

On a quarterly GDP basis they downgraded Q4 from 1% to 0% but the first published forecast for 2026Q1 (they only go out two quarters at a time, beyond the annuals) is 1.8% so they expect a moderate rebound. And by the way, the BoC's forecasts wouldn't include the GST announcement at the start of the week that is estimated to supercharge Q2 income growth and with it consumption growth (recall **here**). MPR and forecasts are finalized well in advance.

PRESS CONFERENCE

The following is an attempt at capturing the Q&A exchange during the press conference. Any errors or omissions are to be blamed on my typing abilities! I will say, however, that CPAC needs to fix its feeds and translation issues.

Q1. Is the BoC saying that the outcome of the USMCA negotiations will dictate the next move in interest rates?

A1. We are saying uncertainty is unusually high. There are a number of risks. Geopolitical risk is high, US trade policy is unpredictable, and for Canada the outcome of the CUSMA negotiations is an important part. We have built into our predictions that current tariffs remain in place. That could change. The uncertainty is already having an impact on the economy which is built into our projection but we have that built into our projections. The outcome may be no change. We have highlighted a number of outcomes for CUSMA. We have published a number of scenarios around different trade configurations.

Q2. You see potential for reallocation of capital. What do you mean?

A2. You have a number of hard hit sectors in Canada. Steel, aluminum, some autos etc. They may need to pivot inside of Canada or outside of Canada with new capital or new skills. Our trade relationship with the US is fundamentally changed. Even if CUSMA is left unchanged, businesses are looking for new markets. I would stress that is going to take some time. It does not happen quickly. Through that transition it does lower the economy's potential. Productivity should come back up but that is going to take some time.

Q3. What has changed since October to say that the range of possible outcomes is wider than usual?

A3. There is a sense that geopolitical risk is heightened. The month of January is pretty packed with new geopolitical risks. US trade policy through last Spring there were big changes with new deals through the summer there was more stability and since then there are new threats. US trade policy remains highly unpredictable. It is 2026, CUSMA is under review.

Q4. Are there implications for monetary policy in Canada if you lose confidence in independent monetary policy in the US?

A4. This threat is contributing to this sense of uncertainty. The Federal Reserve is the biggest and most independent central bank in the world. A loss of independence would affect the world and particularly Canada given its integration. [ed. Macklem then went a little too far in saying Powell is doing a good job imo. They both totally blew it on inflation.]

Q5. Is Trump being vindicated on tariffs in that they are not doing much damage?

A5. [Rogers speaking]. It's too early to tell. Rogers also correctly flagging the coincidental effects of AI.

Q6. Can you update mortgage reset views?

A6. [Rogers again]. We don't have a big change in our views. We do expect those rollovers this year to see payment increases. The recent uptick in the yield curve may marginally add to that risk. Most mortgage borrowers have been prepared for this and mortgage rates have come down. [ed. agreed, micro shock, not macro, doves shouldn't do the same mistake for a third or fourth year!].

Q7. Will the diversification away from the US only partially offset the trade war impacts?

A7. Yes. Macklem repeating Carney's thesis that rules-based trade is over in the US

Q8. What is driving the USD? Are you concerned about recent appreciation by the C$ and would you lean against it?

A8. We don't target the exchange rate. A flexible exchange rate is an integral part of our monetary policy regime. In the last couple of weeks there has been renewed USD weakness. Many currencies including CAD have appreciated on the USD. What's driving it I think is largely geopolitical events. Currencies are not being driven by traditional things like short-term rate differentials or commodity prices. The USD depreciation over the past year has reflected the safe haven role having been dented while other safe havens like gold are up a lot.

Q9. How do you view the cuts in immigration filtering through the economy?

A9. Lower population growth means lower potential growth. [ed. yet the BoC is only lowering it for 2027 as part of their fudging].

Q10. Does elevated uncertainty create a higher burden for moving in either direction?

A10. We did discuss the future path of interest rates. We agreed that the current policy rate is appropriate if the forecast path is realized. The clear consensus was that it's very difficult to predict either the direction or timing of the next move in our policy interest rate. You need to be able to assign probabilities to the risk to assign probabilities to the rate changes. [ed. ie: full-on-neutral for a while as expected]. Is uncertainty higher than it was a year ago? It's hard to parse at every moment in time but it's high. It is important to step back from the daily noise. Some things are clear. It's clear that the era of rules-based trade is over. It's clear that population growth has come down. It's clear than AI will impact. The Canadian economy needs to adjust to these things. It has started. It is going to take some time. If we do adjust then the economy will be more resilient going forward. The central bank is not at the center of that. We can play a supporting role. We are trying to provide some support to the economy while maintaining inflation close to the 2% target.

Q11. What are your main drivers of GDP changes?

A11. Macklem saying they have exports returning to some modest growth along a lower path. We're importing less from the US and exporting more to other countries. [ed. Macklem seemed to cite an old figure for Cdn export share to US, not 75%, actually 67%]. Saying business investment is held back by uncertainty and it's hard to allocate capital. They are starting to adjust to the days of open trade with the US being over. Governments have also increased their infrastructure investment and incentivized business investment.

[ed. Macklem missed an opportunity to tell Canadian businesses to seize the moment in my opinion. See the section on investment my weekly. CAD depreciation offsets mild tariff shock, Canada is the #2 ranked country in the world for foreign direct investment behind only the US, CAD weakness would offset any further tariff shocks versus China that can't with a dirty managed peg, etc etc. In other words, many (not all) Canadian businesses always seem to latch on to excuses not to invest, not to adopt new tech, not to spend on R&D. That's been true for decades.]

RELEASE DATE: JANUARY 28, 2026

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%.

The outlook for the global and Canadian economies is little changed relative to the projection in the October *Monetary Policy Report* (MPR). ***However, the outlook is vulnerable to unpredictable US trade policies and geopolitical risks.***

Economic growth in the United States continues to outpace expectations and is projected to remain solid, driven by AI-related investment and consumer spending. Tariffs are pushing up US inflation, although their effect is expected to fade gradually later this year. In the euro area, growth has been supported by activity in service sectors and will get additional support from fiscal policy. China's GDP growth is expected to slow gradually, as weakening domestic demand offsets strength in exports. Overall, the Bank expects global growth to average about 3% over the projection horizon.

Global financial conditions have remained accommodative overall. Recent weakness in the US dollar has pushed the Canadian dollar above 72 cents, roughly where it had been since the October MPR. Oil prices have been fluctuating in response to geopolitical events and, going forward, are assumed to be slightly below the levels in the October report.

US trade restrictions and uncertainty continue to disrupt growth in Canada. After a strong third quarter, GDP growth in the fourth quarter likely stalled. Exports continue to be buffeted by US tariffs, while domestic demand appears to be picking up. Employment has risen in recent months. Still, the unemployment rate remains elevated at 6.8% and relatively few businesses say they plan to hire more workers.

Economic growth is projected to be modest in the near term as population growth slows and Canada adjusts to US protectionism. In the projection, consumer spending holds up and business investment strengthens gradually, with fiscal policy providing some support. The Bank projects growth of 1.1% in 2026 and 1.5% in 2027, broadly in line with the October projection. A key source of uncertainty is the upcoming review of the Canada-US-Mexico Agreement.

CPI inflation picked up in December to 2.4%, boosted by base-year effects linked to last winter's GST/HST holiday. Excluding the effect of changes in taxes, ***inflation has been slowing since September***. The Bank's preferred measures of core inflation have eased from 3% in October to around 2½% in December. Inflation was 2.1% in 2025 and ***the Bank expects inflation to stay close to the 2% target over the projection period***, with trade-related cost pressures offset by excess supply.

Monetary policy is focused on keeping inflation close to the 2% target while helping the economy through this period of structural adjustment. Governing Council judges the current policy rate remains appropriate, conditional on the economy evolving broadly in line with the outlook we published today. However, uncertainty is heightened and we are monitoring risks closely. If the outlook changes, we are prepared to respond. The Bank is committed to ensuring that Canadians continue to have confidence in price stability through this period of global upheaval.

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.