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GLOBAL ECONOMICS

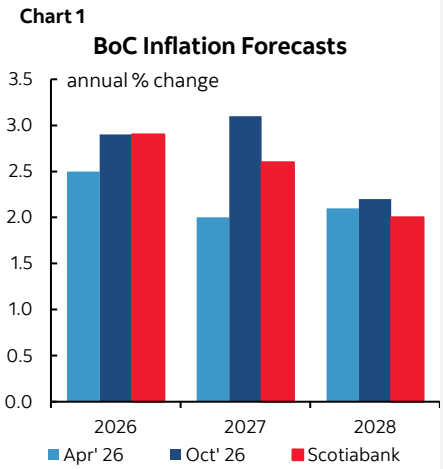
SCOTIA FLASH

October 28, 2026

Contributors

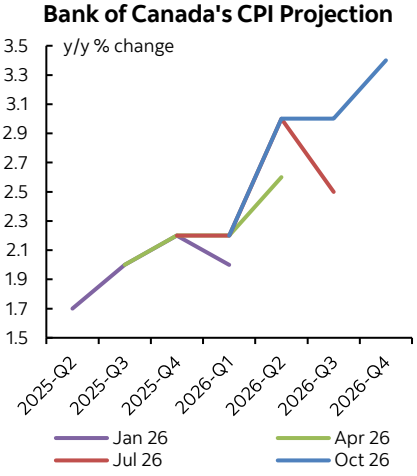
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Chart 1



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

Chart 2



Sources: Scotiabank Economics, Bank of Canada.

Kudos to the Bank of Canada

- **The BoC hiked a quarter point as expected…**
- **…with generally hawkish guidance…**
- **…that supports our forecast for several more hikes to come**
- **It's encouraging that the BoC is dithering less this time**

The Bank of Canada did the right thing today. The statement is **here**, the MPR is **here**, the opening remarks to the press conference are **here**, and the press conference can be watched **here** or **here**.

They raised the overnight lending rate by 25bps to 2.5% as we had long forecast in leading all of consensus and markets. Scotiabank Economics had 2026H2 hikes in our forecasts since November of last year and delayed them to 2026Q4 in January and stuck with it since. This was no lagging shop while everyone else was either talking cuts or no hikes until 2027.

The bias was generally hawkish on the overall suite of communications and forecasts and drove higher market pricing for a follow up rate hike in December that we expect to be delivered. Market pricing for the December move is a 50–50 coin-toss between a hold and a hike. Nothing I heard today sounds like they would wish to pause.

Few like higher borrowing costs, but the BoC is not dithering as it did in the pandemic. Acting today with guidance that broadly points to more hikes ahead means there is a better chance at not having to swallow worse medicine against inflation later. Businesses and households need to understand this since the consequences to letting inflation get out of hand again would be devastating.

The priced path forward is broadly consistent with our 3.25% terminal rate by 2027H1 with more upside than downside risk to this forecast (ie: more, not fewer hikes). Canada's rates curve is underperforming the US curve with a bear flattener move led by a 5bps rise in 2s on the day. The Canadian dollar is little changed on the day partly as the Federal Reserve's decision awaits.

WHAT MADE IT HAWKISH

What made the communications hawkish was a combination of forecasts and the tone.

Key is that they are signalling uncertainty over *when* and *how much* by way of cost pressures get passed through, not *whether* that happens, and doing so by saying: "....and how quickly and fully higher costs will pass through to consumer prices."

Inflation and growth forecasts were revised up—especially a sharp increase in inflation.

There was also zero reference to the jobs report that doves hung their hats on. The very clear signal is that a) it's inflation that they're focused upon, b) they probably don't believe the September jobs report was worthy of being flagged just as much as I don't.

STATEMENT COMPARISON

Key in the statement comparison at the back of this note is the concluding paragraph that guides more hikes are likely to come:

""There could be a need to increase the policy rate further, but given uncertainties, Governing Council agreed to proceed carefully."

When asked during the press conference about this careful wording, Macklem said that policy is not on a pre-set path and there are many uncertainties.

That matched our expectations for what I've described as cagey, circumspect, careful and noncommittal guidance. Why? Because they don't want markets running much further ahead of their plans, yet the broad communications set a more strikingly committed path to policy tightening.

A fuller statement comparison is always less useful when comparing MPR to non-MPR.

THE FORECASTS DID THE TALKING

The opening sentence to the MPR set the tone:

"Inflation in Canada is projected to remain above 3% through much of 2027, materially higher than previously forecast."

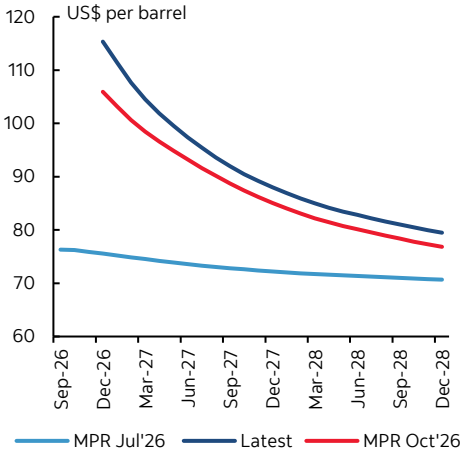
You knew where the rest was going after that deliberately chosen intro.

The inflation forecast was raised to 3.1% in 2027 from 2.0% previously and to 2.2% in 2028 from 2.1%. This is a sustained overshoot of their 2% inflation target.

On a quarterly basis, the BoC now forecasts inflation to end 2026 at 3.4% y/y, end 2027 at 2.6% y/y and end 2028 at 2.1%. Chart 1 shows their forecast compared to ours.

Recall that the BoC's projections will embed an unknown rate profile that presumably incorporates rate hikes. Despite these increases, they are still projecting inflation to overshoot their 2% target and are playing catch up (chart 2). That's a signal they feel they may be behind in fighting inflation and that's a rather hawkish signal. Chart 3 is part of the reason why as the oil futures curve has smashed through what they previously incorporated in their prior forecasts.

Chart 3
BoC's July MPR Brent Oil Assum. vs Latest

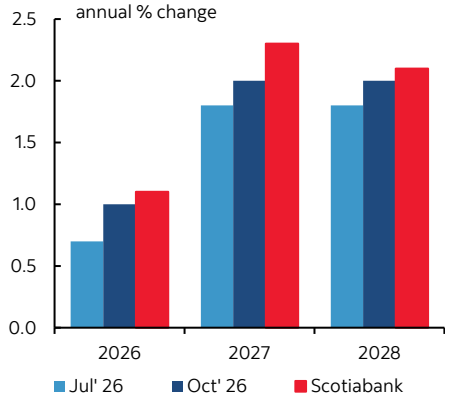


Sources: Scotiabank Economics, Bloomberg.

The BoC rolled out a new model called Prima which no longer forecasts core inflation. They made no effort to provide an alternative means of projecting core inflation. This is a knock against their new approach since there is no accountability in the forecast numbers for how they expect pass through of various inflationary pressures into core baskets.

The growth forecast was raised to 2.0% y/y for real GDP from 1.8% previously for both 2027 and 2028 (chart 4).

Chart 4
BoC GDP Forecasts



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

They incorporated off-budget announcements, pending whatever fresh ones are due next week:

"The projection incorporates information from the latest provincial budgets, the federal Spring Economic Update 2026 and new federal fiscal measures tabled as at October 19, 2026. It includes the expected effects of the Productivity Mega Deduction and activities related to the Major Projects Office."

The BoC left its estimated ranges for forecast potential growth—the economy's noninflationary speed limit—unchanged through the forecast horizon. They expect potential growth to be 1.5% in 2027 and 1.75% in 2028.

Since actual growth is forecast to be above potential growth, the BoC expects slack to close going forward. They estimate the output gap at between -0.25% to -1.25% in Q3 of this year.

PRESS CONFERENCE TRANSCRIPT

What follows is an attempt at providing a general idea of the Q&A part of the press conference after Governor Macklem finished reading his opening remarks.

I have a few comments on some of what follows. Regarding Q2, the answer could have been that the BoC's job is to align supply and demand and so it doesn't matter if it's a positive demand shock or negative supply shock or both. It was the same thing in the pandemic.

Also note that the answer to Q1 sounded like Macklem felt the BoC was holding back on translating the government efforts to stimulate the economy. They'll have another chance in the January MPR when those forecasts incorporate next week's federal Budget.

On forward guidance questions, the reason the BoC is careful is because they learned a harsh lesson against pre-committing in the pandemic by promising to keep rates on hold for years.

On Q11, perhaps the answer should have been that acting now means getting an earlier handle on inflation and therefore hopefully hiking less than if we waited.

On Q13, note that some of the governments that are offering such fuel relief programs are paying a steep price in terms of fiscal deficits.

Q1. How much are federal measures expected to contribute to your growth forecast?

A1. One of the reasons growth is firmer is because of the big projects and mega deduction supports for investment plus high energy prices attracting more investment in the energy sector. I would say we've still been fairly conservative about how much we've increased investment. We've certainly been disappointed in the past.

Q2. What are you trying to accomplish with this rate hike? It won't impact global oil markets or AI so why raise interest rates to deal with this supply shock?

A2. We don't want second round effects. Energy prices have been hig for eight months and look like they're going to stay high and you can see the building cost pressures. Past behaviour shows businesses can absorb higher costs for a while but ultimately they pass them on. By raising the rate we're leaning against pass through and getting back to target more quickly.

Q3. If there is so much concern about inflation risk, why wasn't there a more full-throttled commitment to more rate hikes. Your opening statement says rates "could" move higher.

A3. Uncertainty is high. This is a forecast. It's not the only outcome. We're going to take it one meeting at a time. There is no predetermined path.

Q4. How much judgement did you apply to this decision? Was it a difficult decision? Were the data and everything else making this one a straight-forward call?

A4. You want to look at this through more than one lens. One is through our projections with higher for longer and more persistent inflation. The implication is pretty clear—there is less scope for monetary accommodation. But we are very conscious of the uncertainty around those forecasts, so the other lens is to look through it through a risk management lens. We don't want to increase the policy rate to harm growth if inflation is contained but we also don't want to maintain the policy rate if inflation is less well contained. The balance of risks became more titled toward the latter scenario with inflation being less well contained.

Q5. Do you think you would like to be at the midpoint of neutral as soon as possible?

A5. Neutral is a range, 2.25–3.25%. At 2.25 we're at the stimulative end of that range. We're not going to pre-judge the next decision, we're very mindful of the uncertainty, we're going to take decisions one at a time.

Q6. Are you expecting a slowing in the housing market?

A6. [Rogers now]: Uncertainty, sharper adjustments in Van/Tor are weighing on housing. Higher borrowing costs will weigh a bit on this.

Q7. If inflation is above 2% throughout the middle of 2028 are you signalling rate increases may be needed over the medium term to get on track?

A7. [Back to Macklem] I don't want to get too far ahead. We're going to take this one meeting at a time.

Q8. How did the discussions go? Were there conflicting opinions?

A8. [Rogers]: We debated a hold and a hike. We always do that. There was a very strong consensus and the shift in the risks to inflation drove that.

Q9. Will energy float all boats in the economy or is it just wishful thinking?

A9. Growth in the energy sector is contributing to growth but is not the only driver. The biggest contribution is household spending. Then you've got strength in exports partly driven by the energy sector but not only the energy sector. And business investment is contributing that is partly the energy sector but also the rest of the economy. The energy sector is by no means the only driver of growth.

Q10. Why is the BoC more optimistic about the growth outlook compared to the PBO's outlook?

A10. I can't comment on the PBO forecasts. A first reason is we're getting stronger growth in the middle of the year than expected. We do expect the fourth quarter to be weaker especially driven by tariff effects on small businesses. Looking beyond that we expect export growth, businesses are adapting to tariffs and managing them and finding ways to copy, and when exports go up, businesses invest more to add capacity. Businesses are telling us they're investing more in AI. There have been a number of fiscal measures like the mega deduction.

Q11. Can you explain to businesses how they can deal with higher interest rates when they're already dealing with tariffs?

A11. The best thing that we can do is get inflation down. We can prevent higher energy prices from spreading to other goods and services. By raising our policy rate today, it will help to lean against that pass through. It creates a more stable environment in the future. It's not going to feel good immediately but it's how you get inflation down and that will feel good.

Q12. Is today's hike a response to your delayed COVID reaction?

A12. There is no question we learned from the pandemic. Sicne COVID we've built a new economic model. They are helping us in our need to be more forward looking. Today is nevertheless different from COVID. Coming out of COVID the economy was in excess demand. We have less slack now than a year ago but there is still some slack. That will dampen the pass through. But the cost pressures have gone up, the economy is resilient, we think there will be less slack and inflation risks have increased which is why we increased the policy rate.

Q13. Why raise rates to address the impact of higher energy prices? Some countries in Asia and Europe are providing fuel and electricity subsidies and diversifying energy sources. How would that help?

A13. We're going to leave fiscal decisions to elected governments. The government does have a fuel tax relief program.

Q14. What would have to happen for a single hike to be enough? Is there any historical precedent?

A14. You shouldn't determine that this decision means all uncertainty has gone. We could get a resolution in the middle east but don't think that's imminent. We could get a resolution of trade uncertainty. We need to take our decisions one at a time.

RELEASE DATE: OCTOBER 28, 2026

The Bank of Canada today increased 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%.

Since the July Monetary Policy Report, global economic activity has remained resilient, despite higher energy prices. In the United States, the economy continues to grow at a robust pace, supported by consumer spending and AI-related investment. Growth in the euro area has been resilient and broad-based. After slowing in the second quarter, Chinese growth rebounded in the third quarter, owing to strength in exports and a pickup in fiscal spending. With persistently elevated oil prices and refinery margins, inflation has risen in most countries.

Given the ongoing resilience of the global economy, the Bank has revised up global GDP growth slightly to 3.1% in 2026, while growth in 2027 and 2028 remains unchanged from the July projection at 3.2%.

Global financial conditions have tightened since July. Advanced economy sovereign bond yields are higher. Equity and credit markets have been volatile due to uncertainty about the outlook for the AI sector. The Canadian dollar had weakened somewhat on US-dollar strength but has since recovered to around 71 cents – the same as assumed in the July Report.

Growth picked up in Canada through the middle of the year. GDP growth was 3.3% in the second quarter, and recent indicators point to growth of about 2% in the third quarter. This is stronger than expected in the July Report. Consumer spending has been solid, even with slow population growth. Business investment rebounded, reflecting oil and gas sector activity and spending on machinery and equipment. Despite ongoing weakness in sectors affected by US tariffs, exports overall have strengthened, owing to robust US demand, higher energy production and increasing signs that businesses are adapting to the changing trade environment. The unemployment rate has been around 6½% for several months. A broad set of indicators continue to point to some excess supply in the economy.

Owing to new US tariffs, growth is expected to slow in the fourth quarter of 2026, before picking up again in 2027. This rebound is supported by business investment, exports and fiscal measures. Consumption growth is expected to moderate and housing to remain relatively weak.

The Canadian economy is expected to grow 1% in 2026, and 2% in 2027 and 2028. This is a somewhat stronger overall growth projection than the July Report. This forecast is still subject to considerable uncertainty, particularly regarding Canada-US trade relations.

Given persistently high oil prices, CPI inflation has been around 3% since April and is expected to rise to about 3½% by the end of the year. Excluding gasoline, inflation was 2.2% in September and measures of core inflation remain close to 2%. But cost pressures are building, with high fuel prices raising the costs of production and transportation. Imported industrial and electronics input prices have also increased. While businesses have mostly absorbed higher input costs so far, Bank surveys suggest cost pass-through will increase over the next year. Near-term household and business inflation expectations have risen, while longer-term inflation expectations remain well anchored.

The conflict in the Middle East is now in its eighth month and there is no clear path to resolution. The combination of higher-for-longer energy prices and increased pass-through adds to the persistence of inflation in the projection. CPI inflation is expected to average 3% in 2027, a percentage point above the July projection, then come down to 2% in the middle of 2028. The main sources of uncertainty around this forecast are developments in the Middle East and businesses' responses to cost pressures.

In the outlook, inflation is higher and more persistent than in the July Report. Growth has picked up this year and is expected to recover further. Against this backdrop, Governing Council decided to increase the policy rate to reduce the risk that continuing high energy prices spread broadly to the prices of other goods and services. ***There could be a need to increase the policy rate further, but given uncertainties, Governing Council agreed to proceed carefully.*** The Bank remains committed to maintaining Canadians' confidence in price stability.

RELEASE DATE: SEPTEMBER 2, 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 continuing conflict in the Middle East is keeping energy prices high. As well, new US tariffs and Canadian counter-measures have been announced following the breakdown of trade talks between Canada and the United States. Both situations remain fluid.

In the United States, economic growth continues to be solid, driven by consumer spending and AI-related investment. Growth in the euro area was stronger than expected in the second quarter, while China's economy slowed. Overall, the global economy has shown resilience in the face of geopolitical headwinds, with growth broadly consistent with the July Monetary Policy Report (MPR) projection. With still-high oil prices and elevated margins for refined energy products, inflation in most countries remains high.

Financial conditions have tightened since July. Long-term bond yields have moved up globally, including in Canada. The Canadian dollar has appreciated slightly on US-dollar weakness.

As expected, Canadian economic activity strengthened in the second quarter, with GDP up by 3.3%, following very weak growth in the first quarter. While some of the recent strength reflected temporary factors, the pick-up in activity was broad-based. Consumption showed solid gains. Following several weak quarters, there was some rebound in housing activity. Exports and business investment were up sharply. Labour market conditions have improved in recent months, with the unemployment rate edging down to 6.4% in July. Still, demand for labour remains subdued and indicators point to continued excess supply in the economy.

Overall, recent data reaffirm Governing Council's view of a broadening recovery in Canada's economy. However, uncertainty is high and new US tariffs and threats of further action pose risks to the sustainability of the recovery.

CPI inflation has been hovering around 3% in recent months, mainly because of persistently higher gasoline prices. So far, there has been little evidence of higher energy prices spreading to other components of inflation: excluding gasoline, inflation was 2.2% and measures of core inflation remained close to 2% in July. However, with the Middle East conflict still ongoing and little progress reopening the Strait of Hormuz, upside risks to the Bank's inflation forecast have increased. The longer that high oil prices and elevated refinery margins persist, the greater the risk of spillover to the prices of other goods and services. New US tariffs and Canadian counter-tariffs will also raise costs for some businesses and could feed into consumer prices over time.

With the economy and inflation evolving broadly as forecast in the July MPR, Governing Council agreed to leave the policy rate unchanged. However, the upside risks to inflation have increased, while new tariffs make growth prospects more uncertain. ***Governing Council will assess the sustainability of the economic rebound and the outlook for inflation, and is prepared to adjust monetary policy as needed.*** The Bank remains committed to maintaining Canadians' confidence in price stability through this period of global upheaval.

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