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Tiff Macklem
Governor

Carolyn Rogers
Senior Deputy Governor

Monetary Policy Report - Press Conference Opening Statement

Transcript

Good morning. I'm pleased to be here with Senior Deputy Governor Carolyn Rogers to discuss our policy announcement and the Bank of Canada's Monetary Policy Report.

Today, we raised the policy interest rate by 25 basis points, bringing it to 2.5%. This is the first interest rate increase since July 2023.

There have been two important economic developments since our July Report.

First, the outlook for inflation has deteriorated. With the war in the Middle East persisting, global oil prices have increased and are expected to remain higher for longer. This is hitting Canadians at the gas pump and increasing costs for many businesses.

Second, the growth outlook for Canada has improved modestly, despite continued trade actions by the United States. Growth picked up through the middle of the year, and exports and business and government investment are expected to support a further recovery.

With the outlook for inflation substantially higher and the economy showing resilience, an increase in the policy rate is needed to reduce the risk that elevated energy prices could spill over and become generalized inflation.

We are mindful that uncertainty is still elevated. Developments in the Middle East and Canada-US trade relations both remain fluid. There is also uncertainty about the impact of new US tariffs and how much energy costs will seep into consumer prices more broadly.

Let me expand on what we're seeing in the economy and what we expect in the months ahead.

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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. Consumer spending has been solid, even with slow population growth. Business investment rebounded, reflecting activity in the oil and gas sector and spending on machinery and equipment. Despite ongoing weakness in sectors affected by US tariffs, exports overall have strengthened, bolstered by robust US demand, higher energy production and increasing signs that businesses are adapting to the changing trade environment. The unemployment rate has remained around 6½% for several months. A broad set of indicators continue to point to some excess supply in the economy.

Looking ahead, growth will likely slow in the fourth quarter as new US tariffs weigh on activity. But growth should pick up again in 2027 as consumer spending continues, exports pick up and business investment strengthens, supported by fiscal measures.

Following GDP growth of 1% in 2026, the economy is projected to grow by about 2% in 2027 and 2028. This absorbs the remaining slack in the economy. While uncertainty around the outlook remains high, the growth projection overall is somewhat stronger than in the July Report.

Given persistently high oil prices and elevated refinery margins, CPI inflation has been around 3% since April and is expected to rise to about 3½% by year end. Inflation is projected to remain at or above 3% through much of 2027 before returning close to the 2% target by the middle of 2028. Near-term household and business inflation expectations have risen, while longer-term inflation expectations remain well anchored.

Against this backdrop, Governing Council considered two policy options: hold or hike.

The main argument for holding was that the rise in inflation has so far been concentrated in energy prices and in services that rely heavily on energy inputs, such as airfares. CPI inflation excluding gasoline is still 2.2%, and measures of core inflation remain close to 2%. In addition, while growth has been better than expected, economic slack remains, and new US tariffs will weigh on growth.

The main argument for an increase was that energy prices are higher, they are expected to remain higher, and cost pressures are building. As we've been saying for some time, the longer energy prices remain high, the more likely it is these costs will spill over to consumer prices more broadly.

The prices of gasoline, diesel and heating oil are considerably higher than in July and are expected to remain higher for longer. This is hitting consumers directly and raising business costs for production and transportation. Imported industrial and electronics input prices have also increased. While businesses have mostly absorbed higher input costs so far, past experience and Bank surveys suggest that cost pass-through will increase over the next year. The combination of higher energy prices and pass-through increases the persistence of

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inflation. In addition, with the economy expected to recover, there is less downward pressure on prices to offset these cost pressures.

With elevated inflation expected to last longer and the economy showing resilience, Governing Council agreed that risks to inflation had increased and there was less scope for monetary accommodation. Looking ahead, Governing Council agreed we would take future decisions one meeting at a time. There could be a need to raise the policy rate further, but given the uncertainties, we will proceed carefully.

The Bank remains committed to maintaining Canadians' confidence in price stability through this period of global upheaval.

With that, the Senior Deputy Governor and I are pleased to take your questions.

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