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The Bank of Canada is going back to basics

By Taylor Schleich & Warren Lovely

The release of the federal government's 2026 budget dominated the Canadian news flow last Thursday, but there was another important release that may have been lost in the shuffle: The Bank of Canada and Government of Canada published a joint statement (**link**) on the renewal of the Monetary Policy Framework. Note that a full framework document/ report has yet to be released (**here** was 2021's) but this will presumably arrive soon. At first glance, little has changed. 2% CPI inflation remains the BoC's sole mandate and monetary policy guidepost. Still, there are some notable differences between this renewal and the one in 2021.

What changed? The Bank is no longer instructed to "*actively seek the maximum sustainable level of employment.*" To be clear, the 2021 framework did not give the Bank a formal dual mandate: price stability remained the primary objective, with maximum employment to be pursued "*when conditions warrant*"—in other words, when inflation is low and stable. For much of the past five years, however, inflation was well above target, leaving limited scope to actively pursue this objective.

The new joint statement says that "*monetary policy will continue to be conducted in a symmetric manner, with equal emphasis on deviations above and below the target.*" To us, that's a generous use of "continue to". The 84-page document from 2021 contains exactly zero references to symmetry. (In contrast, the symmetric nature of the target was emphasized up front in the 2016 framework.) Instead, the 2021 mandate reflected concern about *under*shooting the inflation target, noting that the BoC might have to *"[hold] its policy interest rate at a low level for longer than usual.*" Unsurprisingly, that line has also been scrubbed.

There are also no more references to climate change or income inequality, and the joint statement makes no mention of financial regulation or supervision. Finally, the 2021 renewal stated that neutral interest rates "*are likely to be lower than in the past.*" Suffice it to say, that assumption has aged poorly and has also been scrapped.

The 2021 renewal reflected the priorities of the government du jour, but it was also consistent with the broader policy zeitgeist among global central banks. Consider the Federal Reserve. In 2020, the U.S. central bank adopted flexible average inflation targeting, under which it would seek moderately above-target inflation following persistent undershoots, in part to support maximum employment. In 2025, the Fed abandoned that approach and returned to a more conventional framework. (It also pulled back from climate-related initiatives.) To be clear, maximum employment remains one of the Fed's two policy objectives. But the ongoing experience of persistent above-target inflation recentered its priorities, as it did elsewhere. Put simply, central banks are going back to basics.

What's new? The word 'shocks' appears five times in the 770-word statement and the repeated shocks Canada has faced over the past five years clearly inform this renewal. Indeed, the statement stresses that the Bank has strengthened its analytical capacity to better assess how global and domestic supply-side shocks transmit to inflation, and how policy should respond when these are larger and more persistent. The timing of the Bank's new 'Prima' inflation forecasting model, which debuted in the October *Monetary Policy Report*, is therefore not coincidental. Prima, which links sectoral developments to CPI outcomes, provides "a more systematic way to assess where inflation pressures come from, how they spread and how persistent they may become". The framework renewal notes the Bank is "committed to applying these insights with vigilance and clarity".

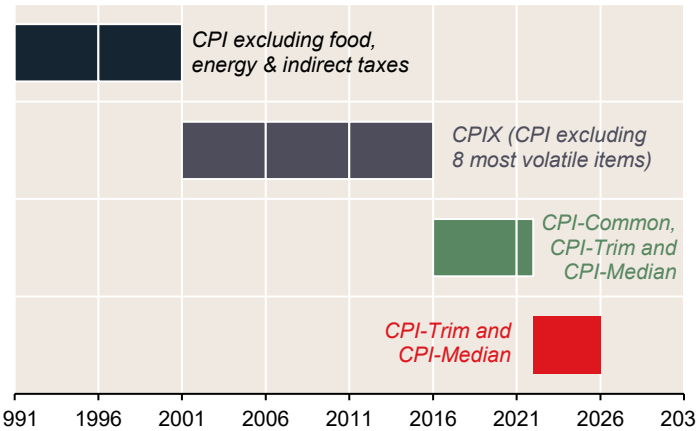
Monetary policy implications: A renewed framework will not suddenly change the course of monetary policy. But it reinforces the message the Bank of Canada has been trying to convey: price stability is paramount. This does not mean the Bank will stop considering domestic economic conditions in its decision-making. But the experience of repeated global shocks and the analytical tools developed in response imply it will place greater emphasis on how external shocks pass through to domestic prices. The latest decision was consistent with this shift: the Bank raised rates despite economic slack, job market softness and relatively contained core inflation because it judged that higher energy costs would broaden into other prices. The accompanying MPR explained that this pass-through is likely to keep inflation above target for much of the next two years. Unless that assessment changes materially, the Bank may struggle to justify delaying further near-term tightening.

What about core inflation? The joint statement says nothing about core inflation, but the full framework document may shed light on how the Bank intends to measure underlying price pressures. We have been critical of the Bank's frequent changes in this arena. In 2021, the Bank had three preferred measures and identified CPI-common as the best performer across several criteria. But before long, this measure was discontinued, leaving just CPI-Trim and -Median. The Bank later began distancing itself from these measures, judging that they misrepresent underlying inflation. Then, in last week's *Monetary Policy Report*, it discontinued its core projection (the average of CPI-Trim and -Median) without explanation.

This leaves us speculating about whether the Bank will adopt a new core measure, multiple measures or no preferred measure at all in its seemingly endless search for the best gauge of underlying price pressures. We've argued (**here**) that the Bank should commit to a single exclusion-based measure, such as CPI excluding food and energy, as most central banks do. In the spirit of going back to basics with its mandate, perhaps the Bank will do the same with core inflation. Prima's component-level detail could make a fixed-exclusion measure a natural complement. But whether the BoC chooses that path remains to be seen.

Chart: Core inflation has been an evolving concept

Timeline of Bank of Canada preferred core measures by year



*Source: NBC, BoC | Note: See our **Special Report** for more on the BoC's core inflation saga.*

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