The World and Australia: Economic & Policy Outlook

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ECONOMICS UNCHAINED
INDEPENDENT ANALYSIS & INSIGHTS

Key Global Factors

The global economy – Resilience amongst uncertainty

- The US has elected a ‘disruptor’ to the White House.
- The desire to ‘make America great again’ will impact the global economy given the complex interconnectivity of the global trade, investment, financing and supply chains.
- But, in July 2025 the IMF upgraded the global growth outlook to 3.0% for 2025 (previously 2.8%) and 3.1% for 2026 (previously 3.0%). But this is slower than the 3.3% achieved in 2024.
- US growth expected to slow noticeable from 2.8% in 2024 to 1.9% in 2025 (up from the April 2025 forecast of 1.8%) and 2.0% in 2026 (up from the previous forecast of 1.7%).
- Growth in China is forecast to slow to 4.8% in 2025 from 5% in 2024 and slow further to 4.2% in 2026.

Source: IMF World Economic Outlook, July 2025

The global economy – Tariffs are a tax

- Tariffs are a tax on the consumer of the importing nation, ie. like a GST/VAT. Tariffs are paid by the importer at the port of destination.
- Tariffs increase prices of consumer goods and add upward pressure to inflation.
- Tariffs disrupt the global supply chain and raise the cost of doing business – reducing the incentive to employ.
- But the US tariffs are expected to raise ~$US2.5-$US3trn in revenue over the coming 10 years – which will partly offset the increase of ~$US3.5trn to the US budget deficit from the OBBB.

Figure 2. U.S. Average Effective Tariff Rate Since 1790

Customs duty revenue as a percent of goods imports

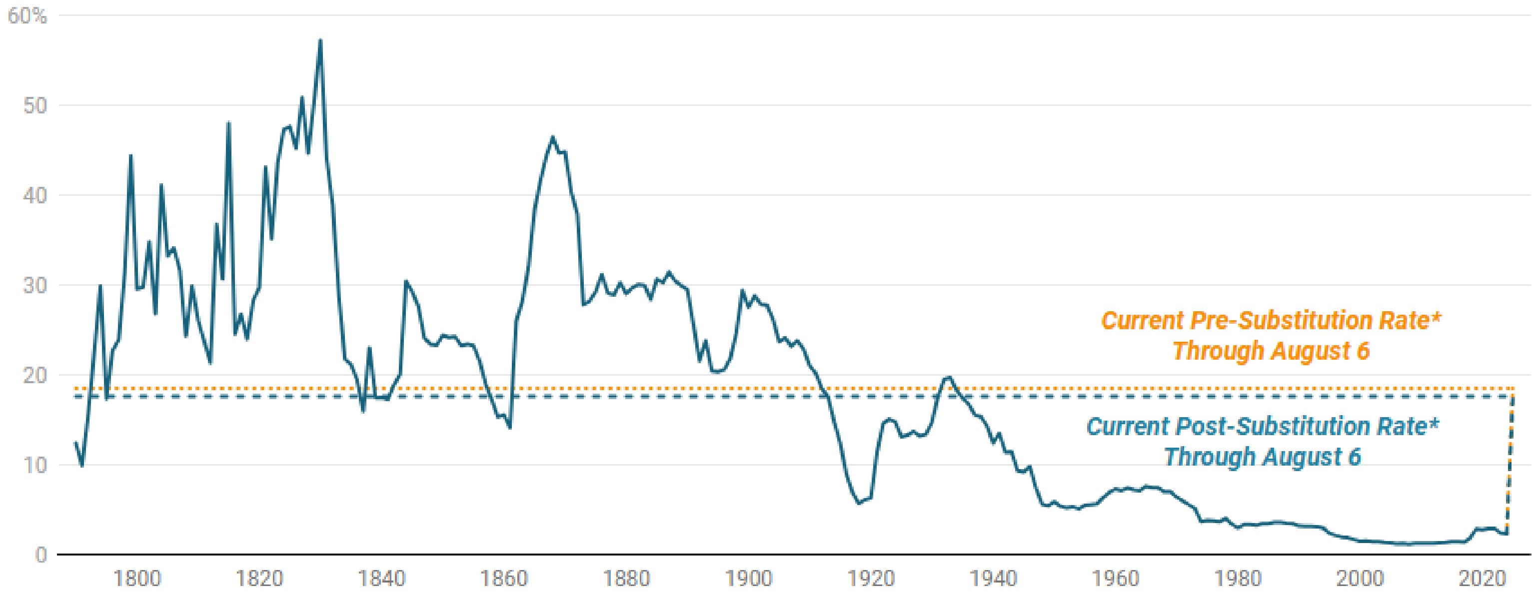
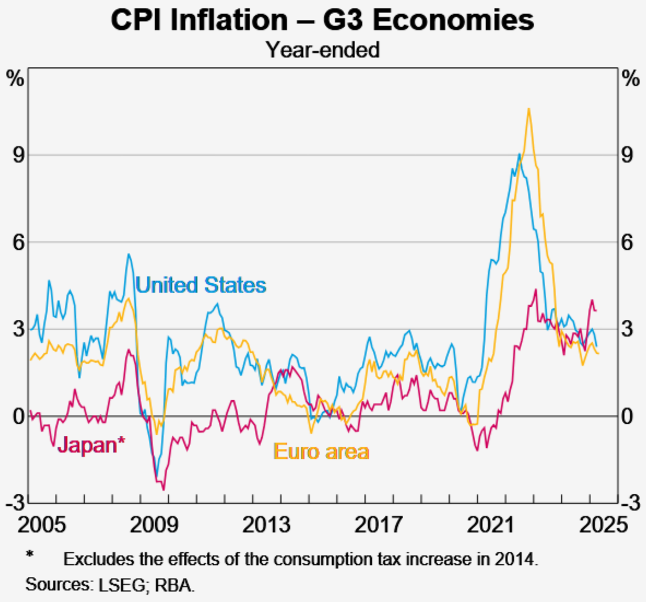


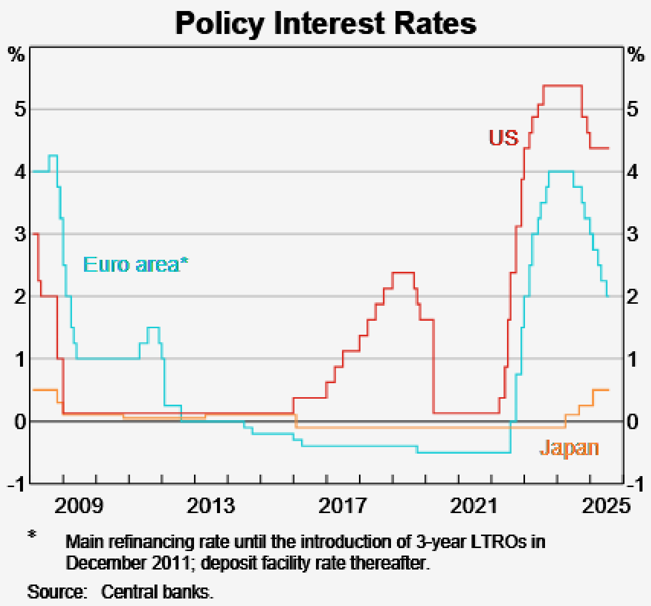
Chart: The Budget Lab • Source: Historical Statistics of the United States Ea424-434, Monthly Treasury Statement, Bureau of Economic Analysis, The Budget Lab analysis. • Created with Datawrapper

Source: The Budget Lab – Yale University

The global economy – Inflation and interest rates

- Inflation in the major economies was converging back to the 2% target – but risks are tilted to the upside in the US (rise to 2.9%/yr in August).
- The IMF forecasts inflation in the advanced economies at 2.5% in 2025, from 2.6% in 2024 and a peak of 7.3% in 2023. Inflation expected to moderate to 2.1% in 2026.
- Except for Japan, lower inflation has allowed major central banks to cut interest rates
- The US Fed has been much more cautious and is confronting hostility from President Trump.
- But the Fed Chair has recently signalled that rate cuts should resume in September – expect ~100bp of rate cuts over next 6mths ie. Trump gets what he wants from the Fed.

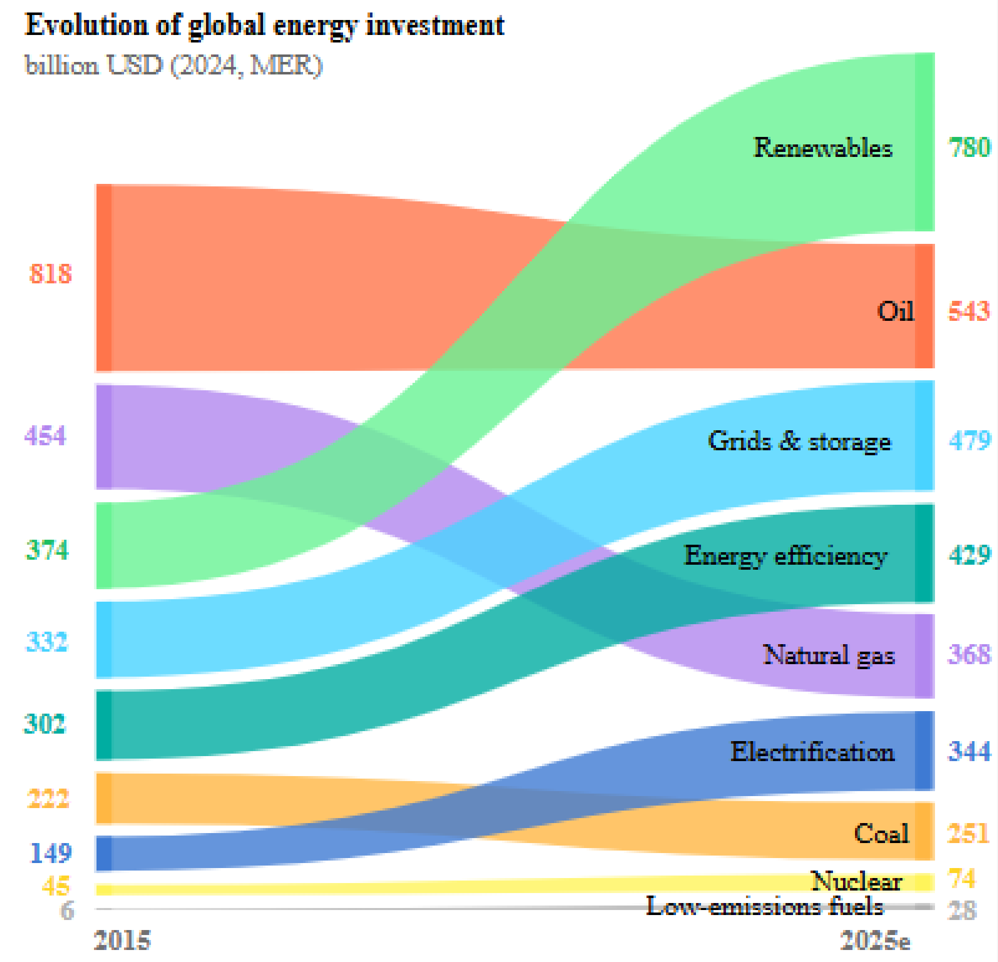




Source: RBA Chart Pack, August 2025

The global economy – Sustainability a key focus

- While the world deals with the near-term risks of tariffs, growth and inflation – the longer run challenge of Climate Change remains.
- The International Energy Agency (IEA) reports that in 2025 global energy investment is estimated at $US3.3trn, with $US2.2trn on clean energy and $US1.1trn on fossil fuels.
- In 2015 total energy investment was closer to $US2.5bn, with $US1.1bn on fossil fuels and $US1.1bn on renewables.
- The increase in investment on renewables will/must increase to reach the net zero carbon by 2025 targets.

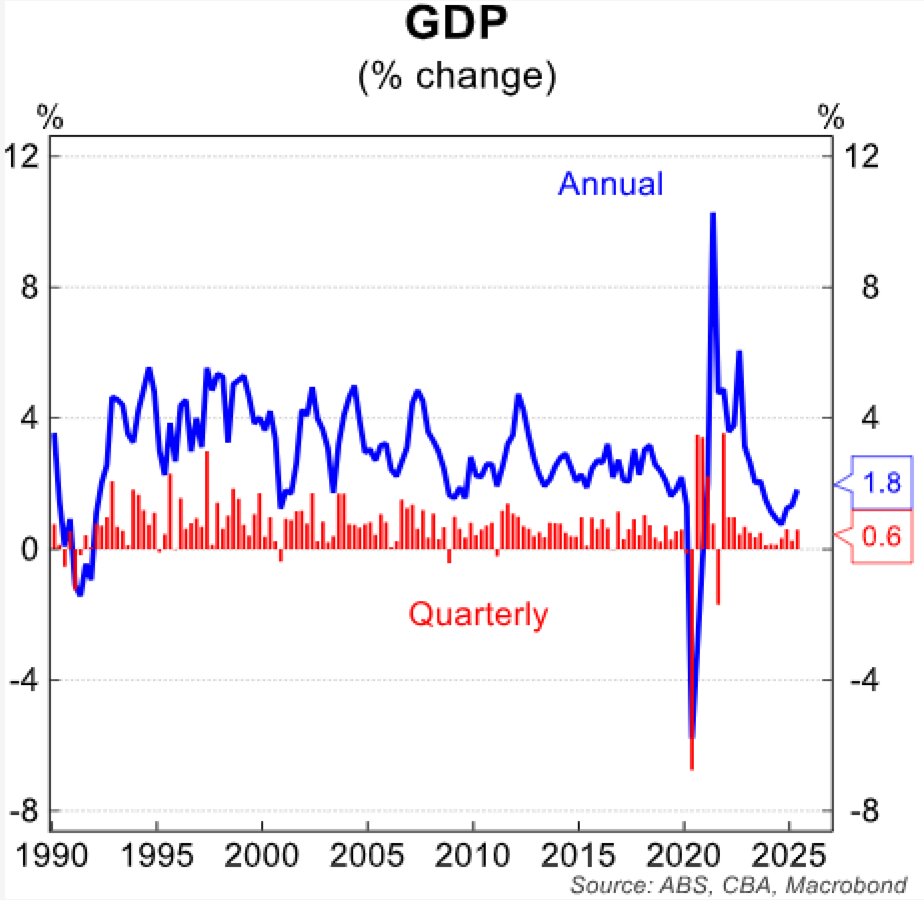


Source: International Energy Agency. June 2025

Australia

Australia – Better momentum into mid-2025

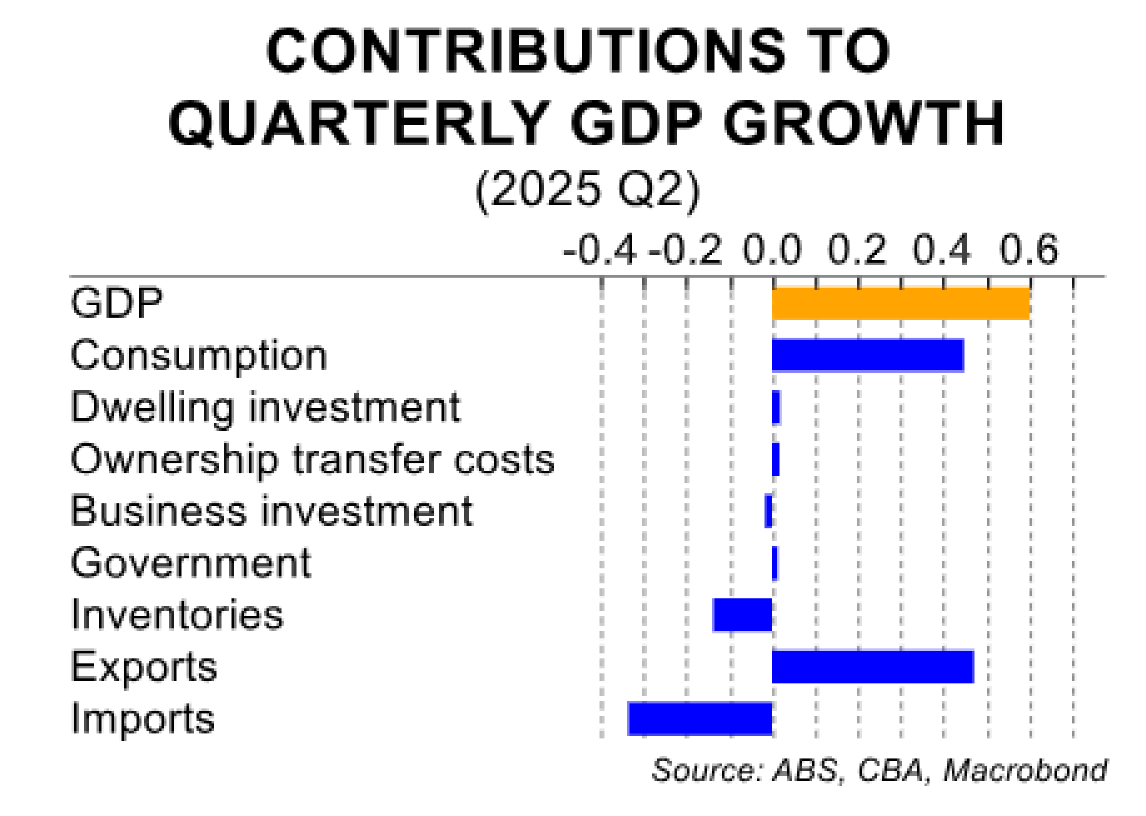
- The Australian economy picked up momentum into mid-2025.
- GDP rose 0.6%/qtr in Q2 25 GDP, up from 0.3%/qtr in Q1 25, taking the annual growth rate to 1.8%/yr from 1.4%/yr previously.
- The primary source of growth shifted to private consumer spending and away from government (both C'wealth and State) spending.
- The RBA was expecting GDP growth of 1.7% as at Q4 2025 – which may need to be revised higher. Growth of 2.1%/yr is forecast at Q4 2026 and then 2.0%/yr as at Q4 27.
- While this is a strengthening of growth – it remains well below the long-run average of ~2¾%.



Source: CommBank Economics, 3 Sept 2025

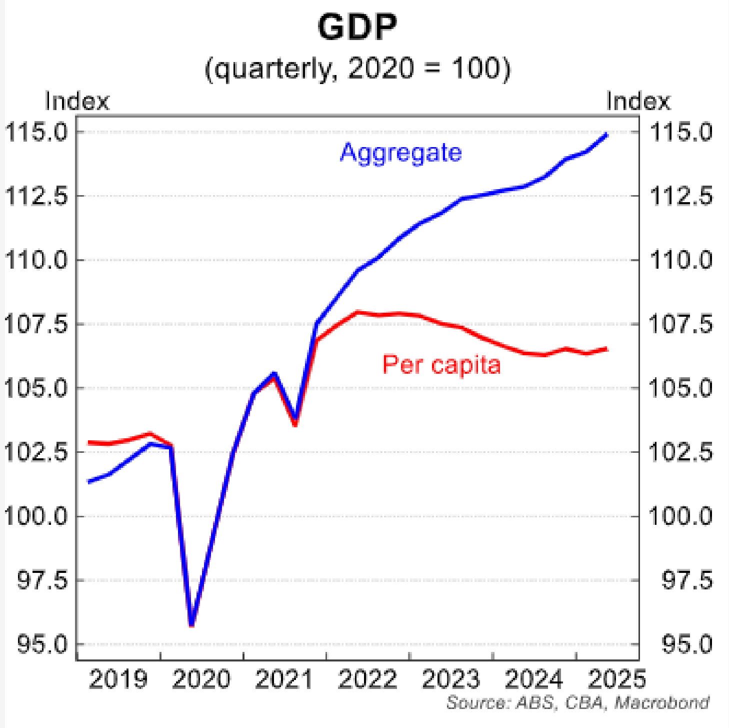
Australia – Growth switches to private sector

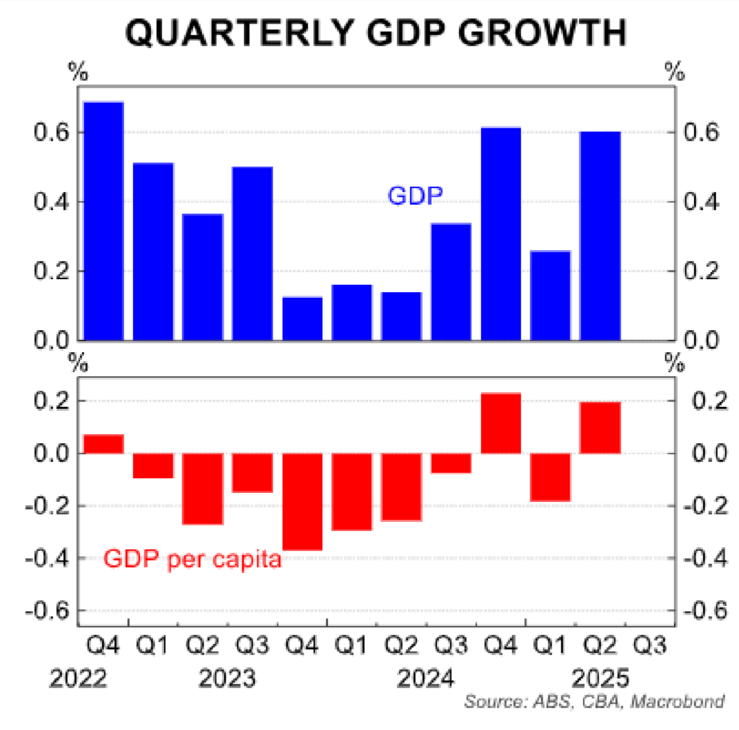
- The largest contributor to economic growth in 2024 and Q1 25 was 'government' – both C'wealth and State – specifically related to the 'care economy' (ie. NDIS) and Infrastructure spending.
- But for Q2 25, the strongest source of growth was private consumption (up 0.9%/qtr) – supported by ANZAC Day and Easter holidays being close to each other and a rebound in Qld after the big weather events.
- Dwelling investment provided a small contribution to growth (0.4%), while business investment was close to balance (-0.1%) and net exports were a small positive (+0.1%).



Source: CommBank Economics, 3 Sept 2025

Australia – Per capita growth begins to turn up



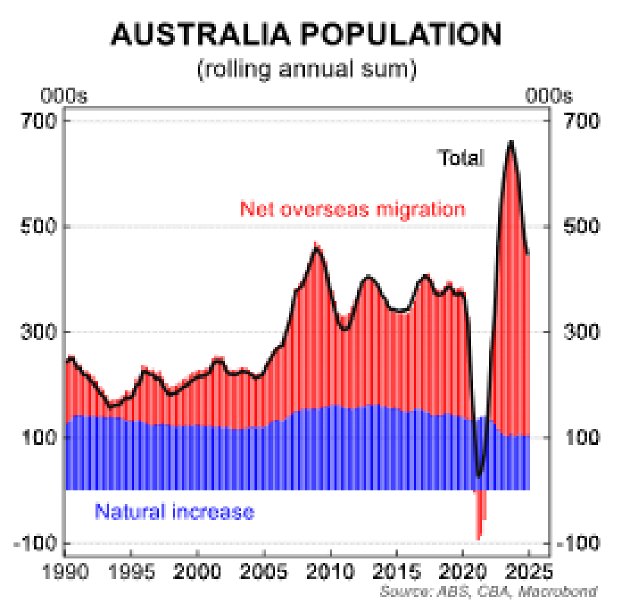


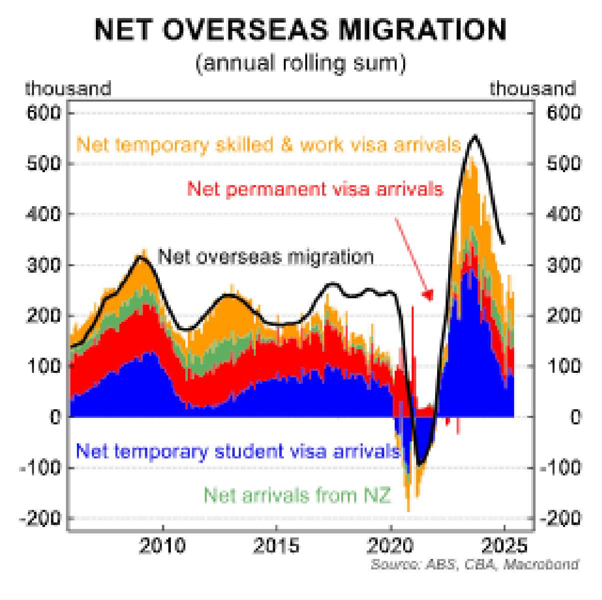
Source: CommBank Economics, 3 Sept 2025

- GDP per capita rose 0.2%q/yr in Q2 25, as the economy grew by 0.6%/qtr and population growth was 0.4%/qtr.
- Real GDP per capita has only increased three times in the past 11 quarters.
- Real GDP per capita is still -1.3% below its peak of Q2 22.
- Income per capita rose by 0.1%/qtr in Q2 25 but also remains well below its 2022 peak.

Australia – Population growth slowing after a surge

- Australia's population growth rate was relatively stable from 2015-2019 and then dropped sharply through the pandemic.
- In 2022 population growth rose to 0.8%/yr and then surged to 1.6% in 2023 and 1.7% in 2024.
- Population growth is now slowing again, driven by a slowdown in international students.
- A slower population growth rate could limit nominal GDP growth but will continue to support an improvement in per capita growth.

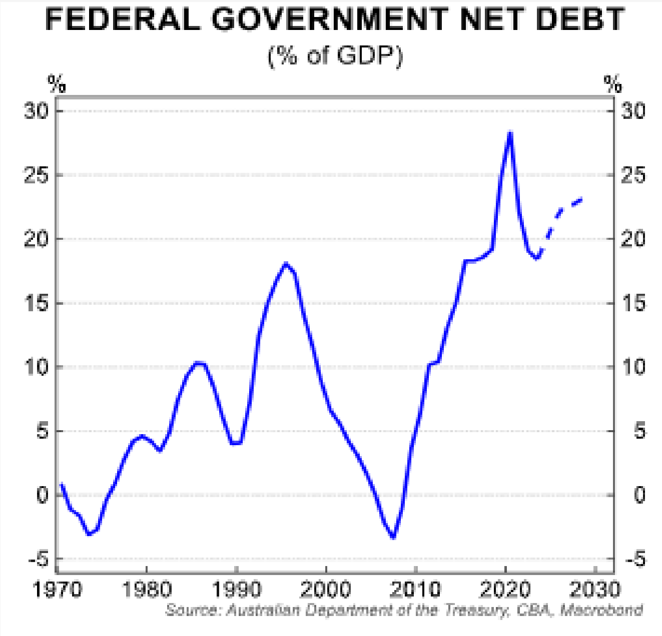


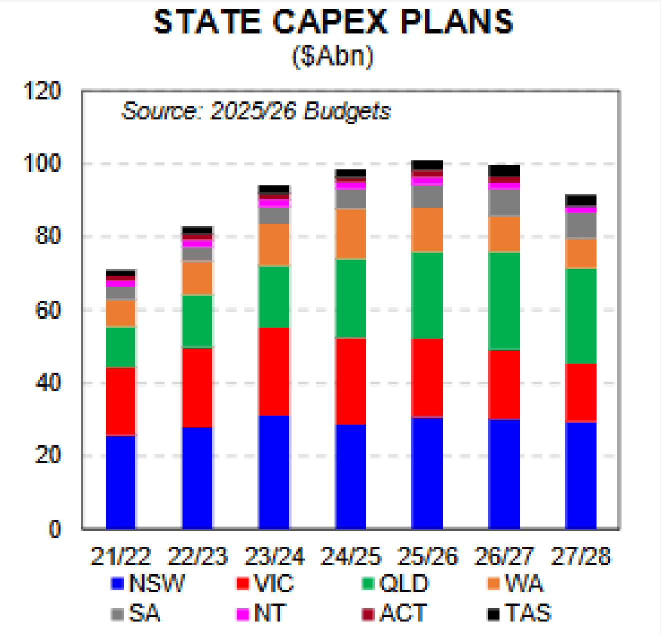


Source: CommBank Research, 19 June 2025

Australia – Fiscal policy expansionary

- The 2025/26 C'wealth Budget (released before the election) showed a deterioration in the fiscal outlook out to 2028/29.
- Net debt of the C'wealth will rise to 23.1% of GDP by June 2029, up from an estimated 19.9% of GDP at June 2025.
- While this remains low by global standards, the increase is a worrying trend.
- This will see fiscal policy provide an expansionary impulse to the economy in the years ahead.
- State govt budgets show that Capex plans (ie. infrastructure spending) will remain high in 25/26 and 26/27, before beginning to moderate on current plans.

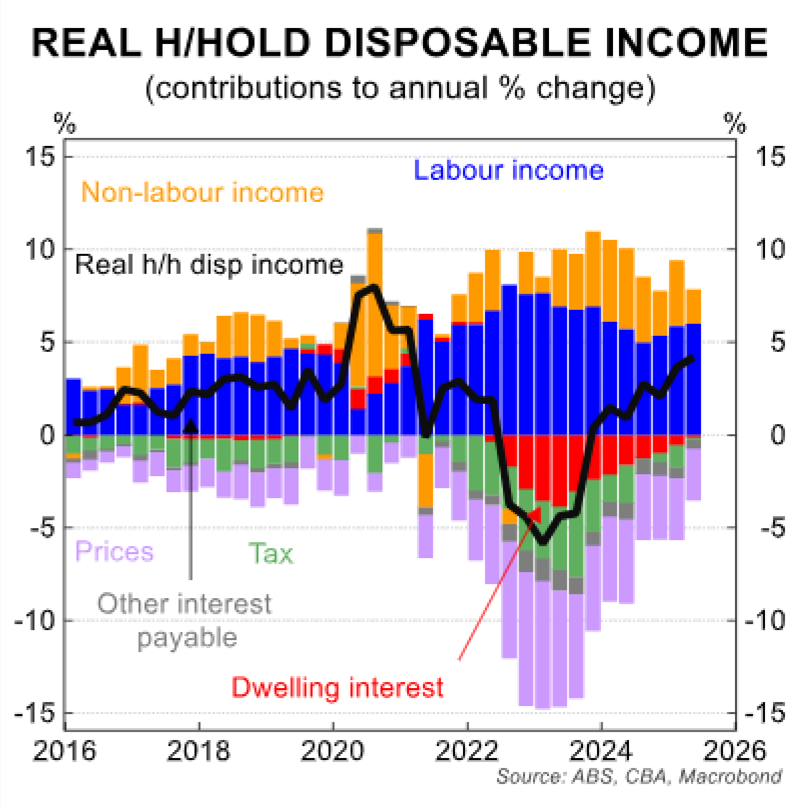




Source: CommBank Economics, 26 March and 2 July 2025

Australia – Real household disposable income now up

- Australia has been experiencing one of the worst outcomes of the major economies in real income growth.
- This was Australia's 'cost of living' crisis!
- While nominal income growth from labour has been strong in recent years, this had been more than offset by higher prices, higher taxes and higher interest rates.
- But, the annual rate of increase in real household disposable income rose to 4.2%/yr in Q2 25 – the strongest rate since Q1 21.
- The improvement in real household disposable income is being driven by lower interest rates, as well as the benefit of the Stage 3 income tax cuts.
- At the same time, labour income remains solid – as does non-labour income (ie. govt payments).



Source: CommBank Economics, 3 Sept 2025

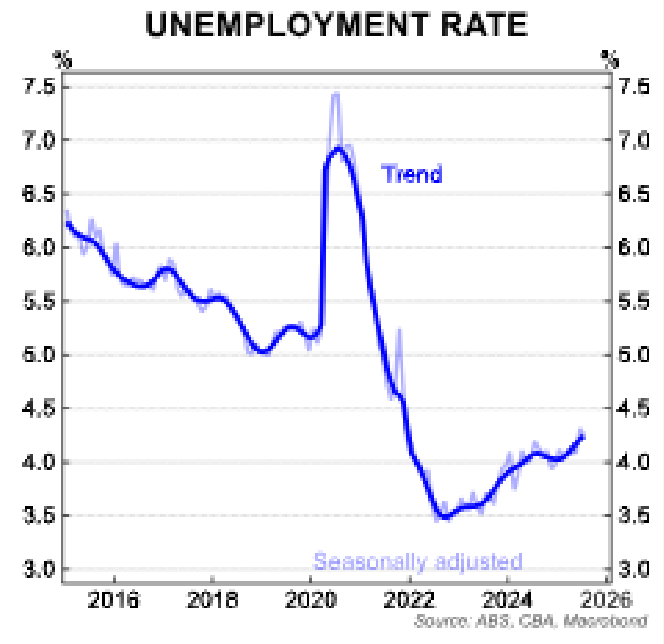
Australia – Consumer spending begins to improve

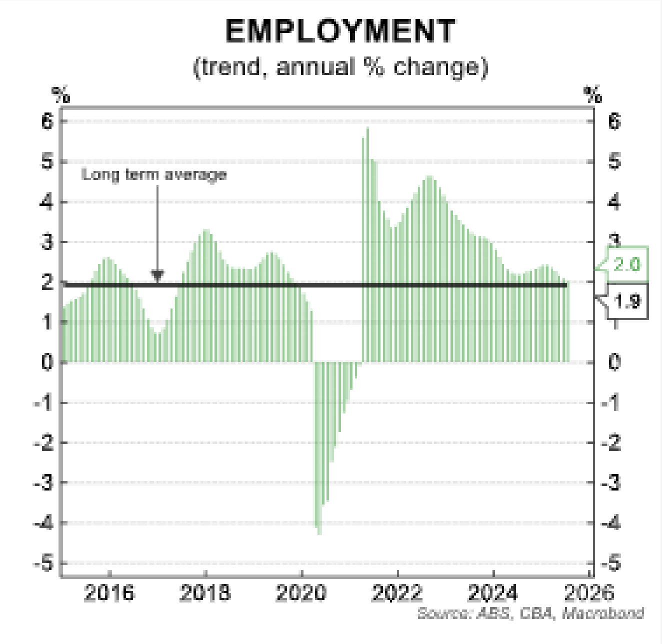
- The Australian consumer had been very soft for much of 2024 and the start of 2025 – weighed down by higher prices and weak real household disposable income.
- But monthly retail trade data for June showed a surprise increase of 1.2%/mth – driven by end of financial year sales and a rebound in Qld after Cyclone Alfred, to be up 4.9%/yr.
- For Q2 25, real retail spending was up 0.3%/qtr and 1.5%/yr.
- But real retail spending per capita was flat in Q2 25 and down -0.1%/yr.
- The RBA will need to keep cutting interest rates through 2025 for consumer spending to improve significantly.

Source: CommBank Economics, 31 July 2025

Australia – Labour market holding in

- Employment increased by 24.5k in July – after being relatively flat in May & June.
- With the participation rate near a record high at 67.0% the unemployment rate edged down to 4.2% in July.
- The unemployment rate has now been 4%-4¼% for over a year.
- Employment growth is showing some signs of moderation – as non-market sector employment growth slows.
- The RBA will be very alert to any signs of a weakening in the labour market.

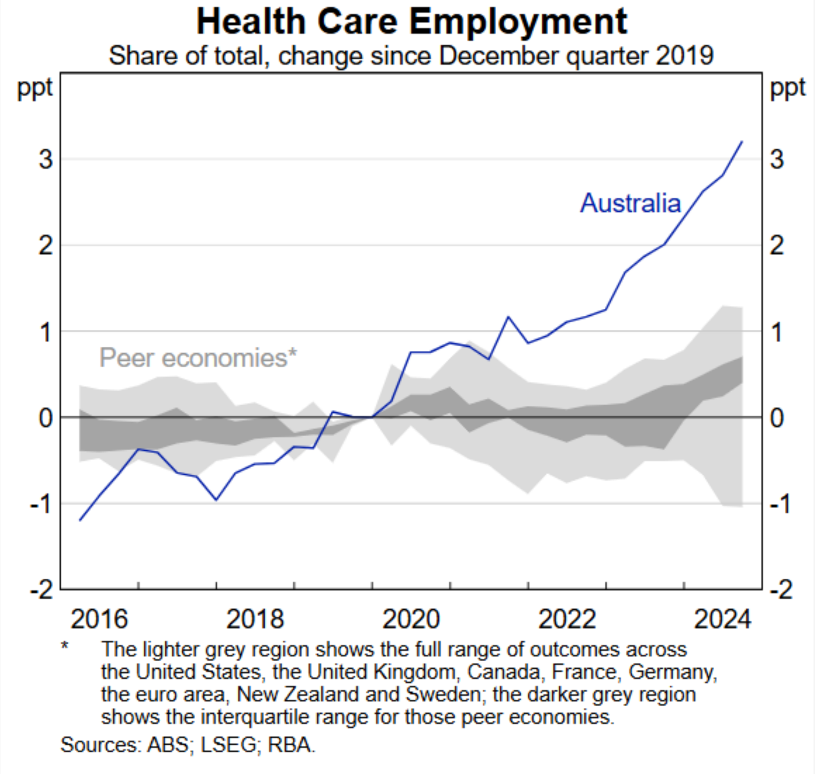




Source: CommBank Economics, 14 August 2025

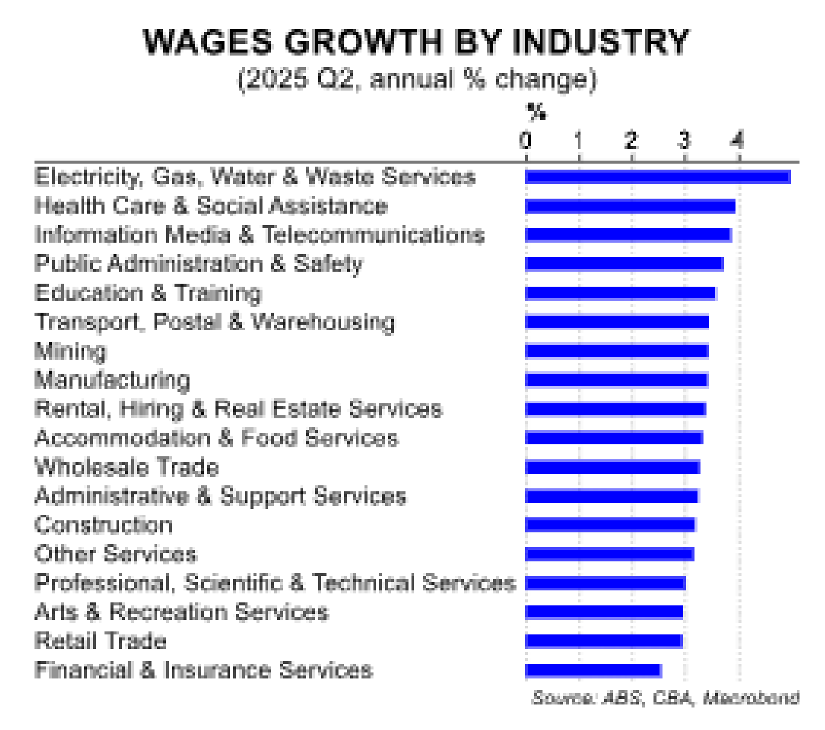
Australia – Employment driven by health sector

- Much of the (surprising) strength in employment in Australia was due to a surge in jobs in the 'non-market sector' - namely health care.
- The increase in health care employment accounted for about half of all employment growth in 2024.
- The strength in health care employment in Australia has been significantly stronger than other advanced nations.
- The NDIS is the primary driver of this phenonium.



Australia – Wages growth steadying

- Wages growth slowed marginally to 0.8%/qtr in Q2 25, leaving the annual rate steady at 3.4%/yr.
- Wages growth continues to be supported by back-dated pay rises in the state public sector and other scheduled pay increases in the care economy.
- Private sector wages rose 0.8%/qtr and 3.4%/yr in Q2 25, with the public sector up 1.0%/qtr and 3.7%/yr.



Source: CommBank, 13 August 2025

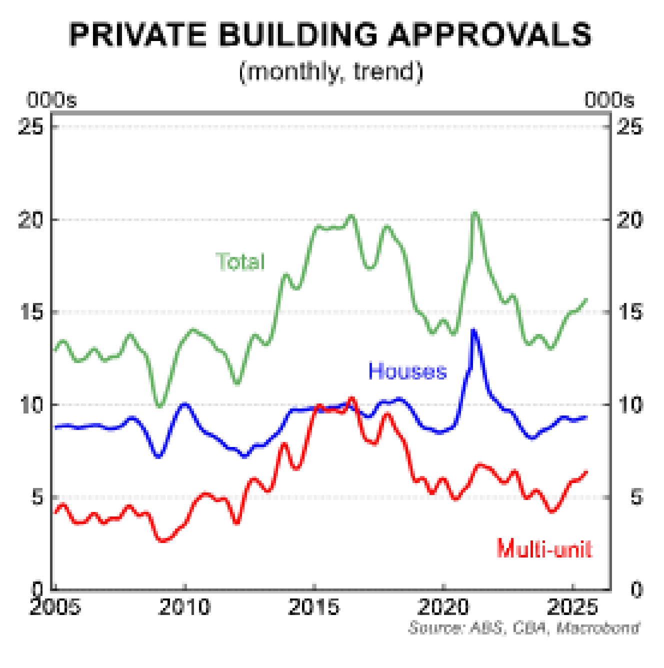
Australia – Productivity is weak, but improving

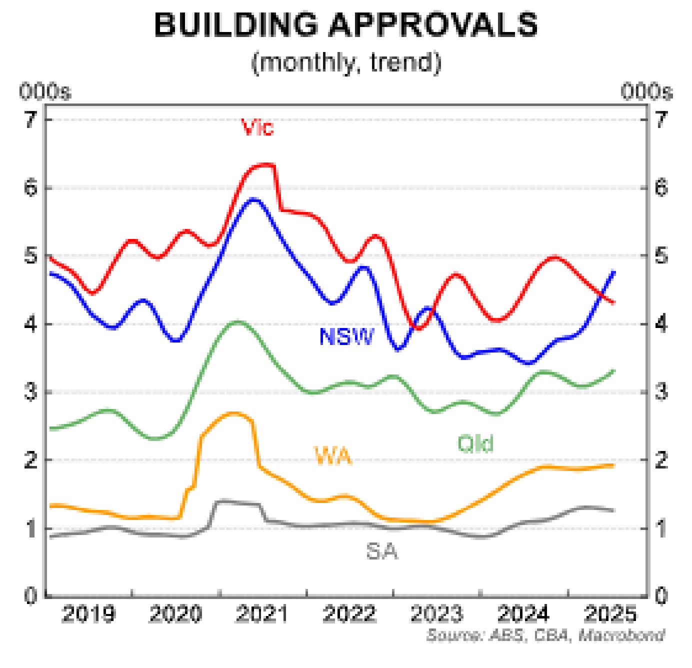
- Australia's productivity rose 0.3%/qtr in Q2 25, after being flat in Q1 25, but remains weak overall.
- Labour productivity is around its pre-pandemic levels.
- Low productivity has a significant impact on consumption growth.
- Policies that could help include:
  - Education and skills training
  - R&D development
  - Lower energy prices through the transition
  - Better use of technology/AI
  - Reduced regulation – red and green tape
  - Labour market reforms to increase flexibility
  - Infrastructure investment
  - Increased competition/reduced market concentration
  - Tax reform – increase and broaden GST/lower income and company tax

Source: CommBank Economics, 3 Sept 2025

Australia – Housing approvals beginning to lift

- After being very weak through much of 2023 and 2024 – residential approvals are now lifting.
- Approvals fell by 8.2%/mth in July, but this followed a 12.2%/mth increase in June. The annual rate of increase is 6.6%/yr.
- The gains and volatility is being driven largely by higher-density housing (ie. apartments).
- Approvals for housing remains soft.
- The government is targeting 1.2m new dwellings over the next 5 years or 240k/yr.
- The current run-rate is ~189k per year, an improvement from lows ~150k, but still well short of what is required.
- There has been a recent strong improvement in NSW, while Vic is falling back after previous strength.



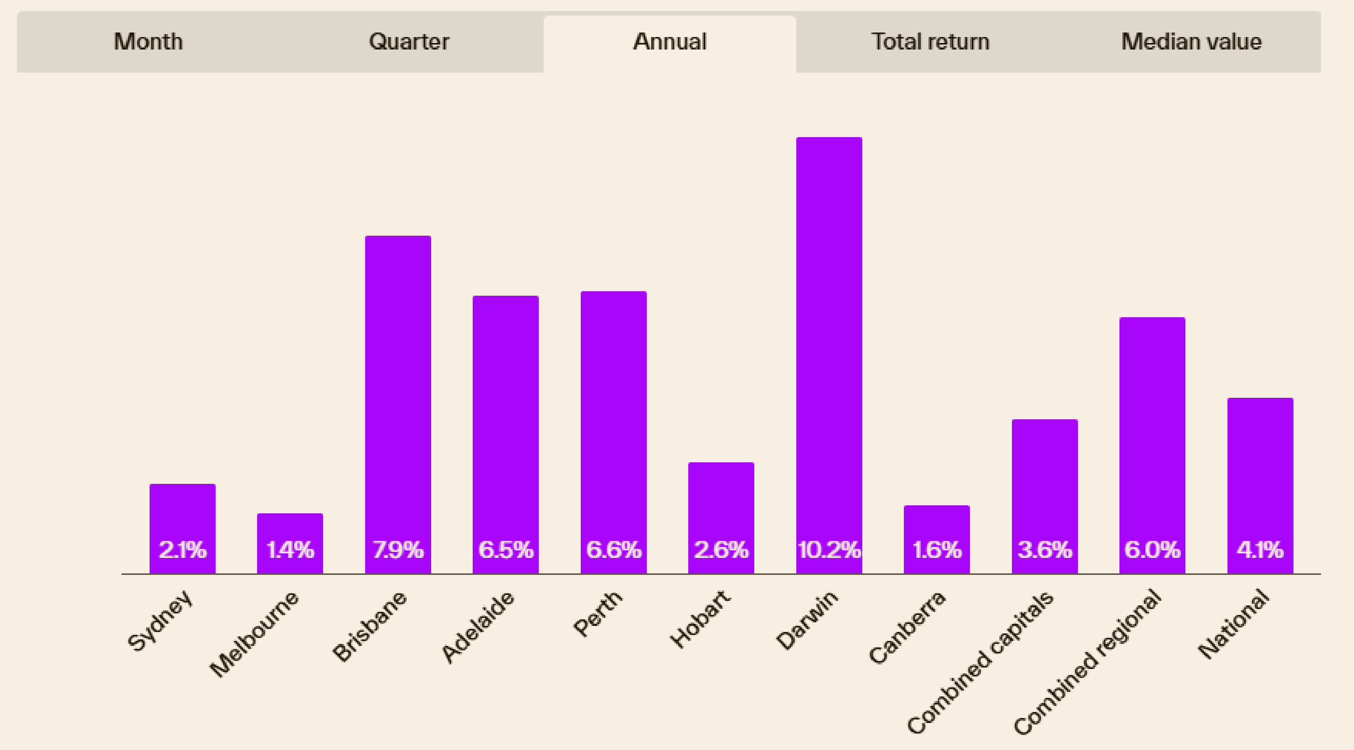


Source: CommBank Economics, 1 September 2025

Australia – House prices picking up again

- After moderating in early 2025, Australian house price growth is beginning to accelerate again – supported by RBA rate cuts.
- Prices rose 0.7%/mth and 4.1%/yr nationally in August Taking the median house price to $A848.9k.
- Brisbane led the gains in August (1.2%), followed by Perth (1.1%), Darwin (1.0%), Adelaide (0.9%), Sydney (0.8%), Canberra (0.4%) and Melbourne (0.3%). Hobart was down -0.2%.
- Over the year to August the largest increases were Darwin, Brisbane, Adelaide and Perth.

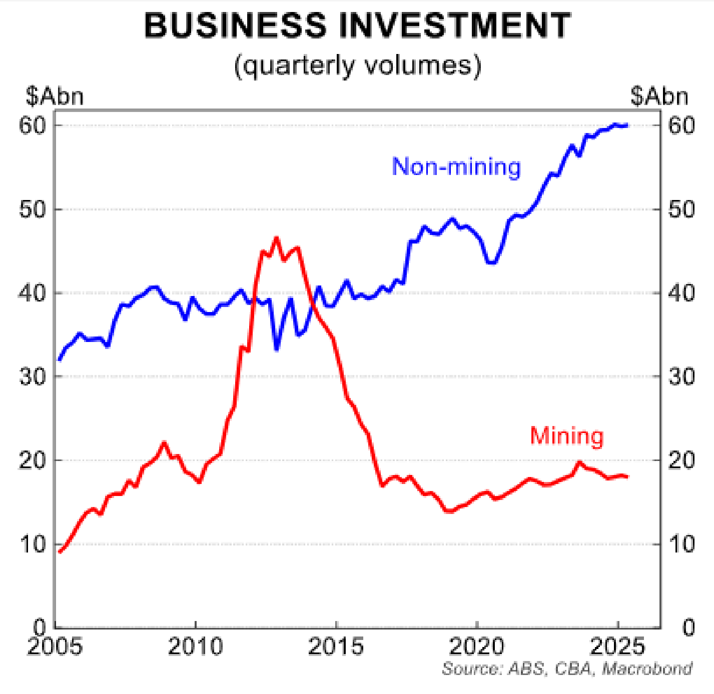
Annual % change in residential prices – to August 2025

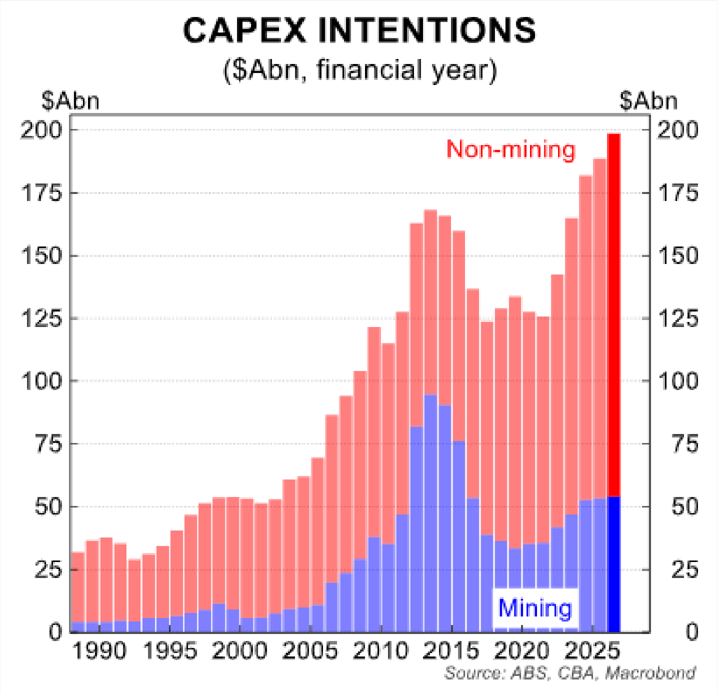


Source: Cotality, 1 September 2025

Australia – Business investment remains soft

- Business investment remains subdued, both in outright levels and as a share of GDP.
- The total volume of capex rose just 0.2%/qtr in Q2 25 – after a fall of -0.2%/qtr in Q1 25.
- Non-mining capex rose by 0.9%/qtr in Q2 25, while mining was down -1.4%/qtr.
- FY25 total capex is expected to be up 3.8%/yr, with FY26 capex estimated at up ~5%.
- Low capex spending and plans fits into the low productivity story and needs to improve.

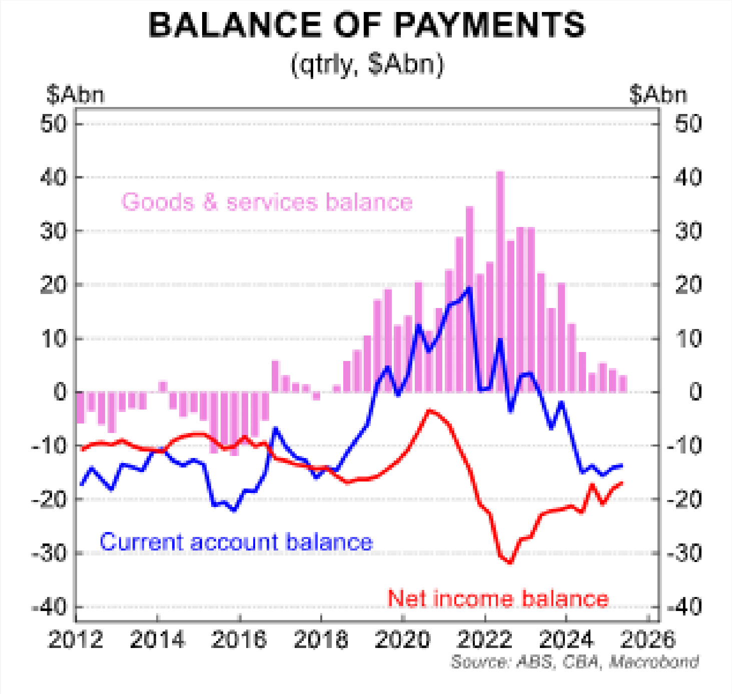


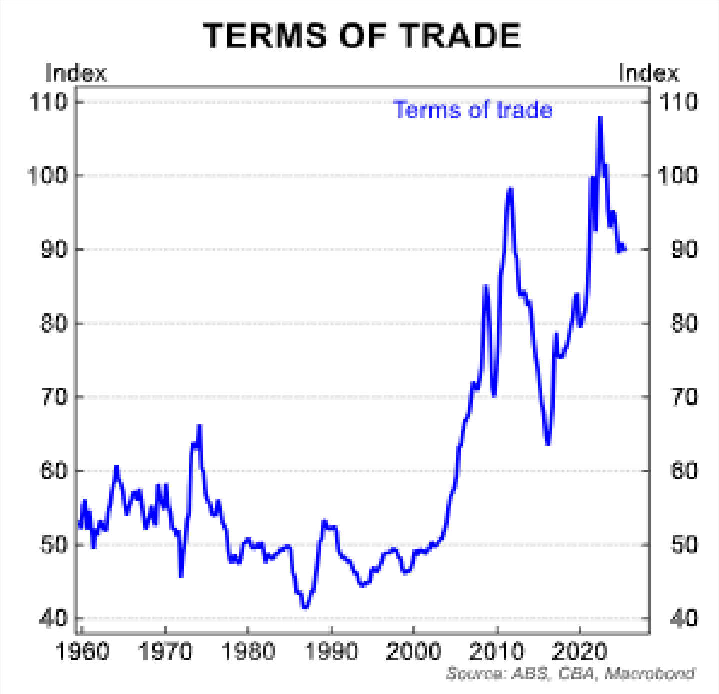


Source: CommBank Economics, 3 Sept 2025

Australia – Export growth softening with prices

- The export of resources has been strong in recent years, driven by both iron ore and LNG – but are flattening out as prices adjust lower.
- Services exports (inbound tourism and education) have bounced back strongly.
- The net export sector made a small positive contribution to economic growth in Q2 25.
- China is the largest export market at ~30%. The next largest are Japan and Sth Korea. The US accounts for only ~5% of exports.

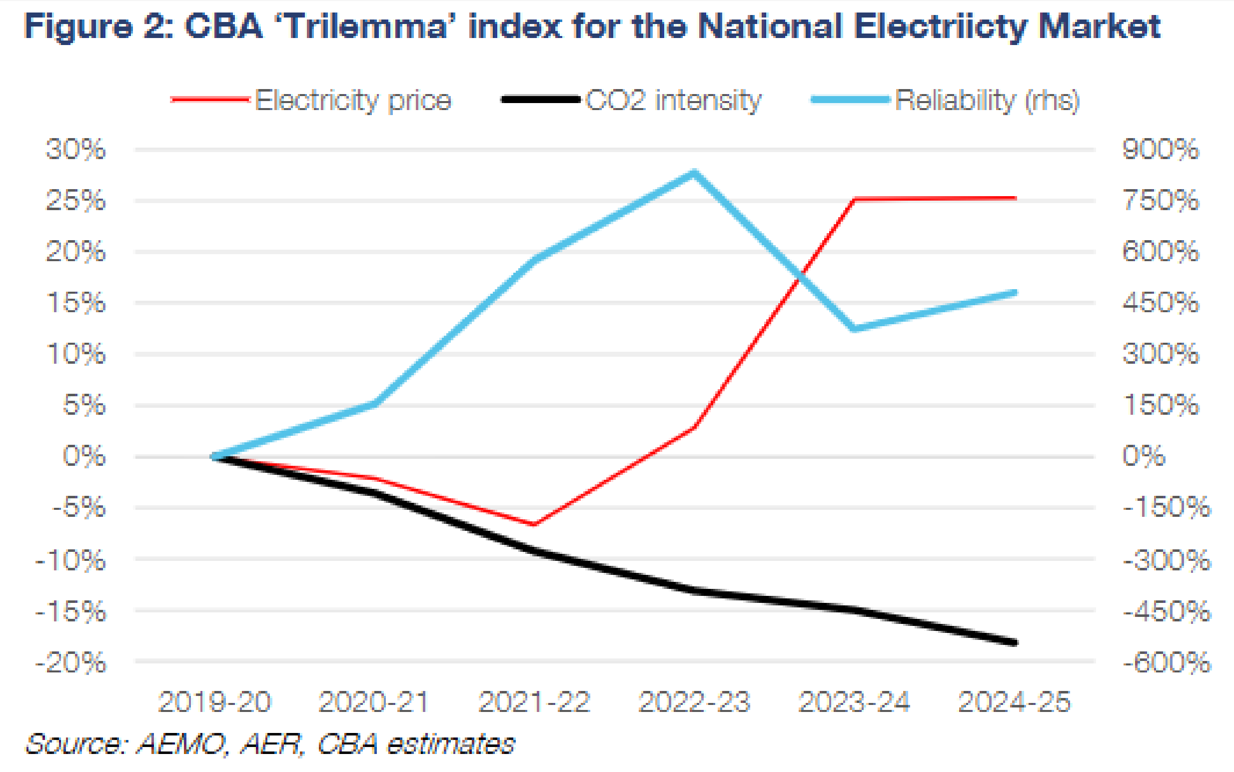




Source: CommBank Economics, 2 September 2025

Australia – Energy transition is a challenge

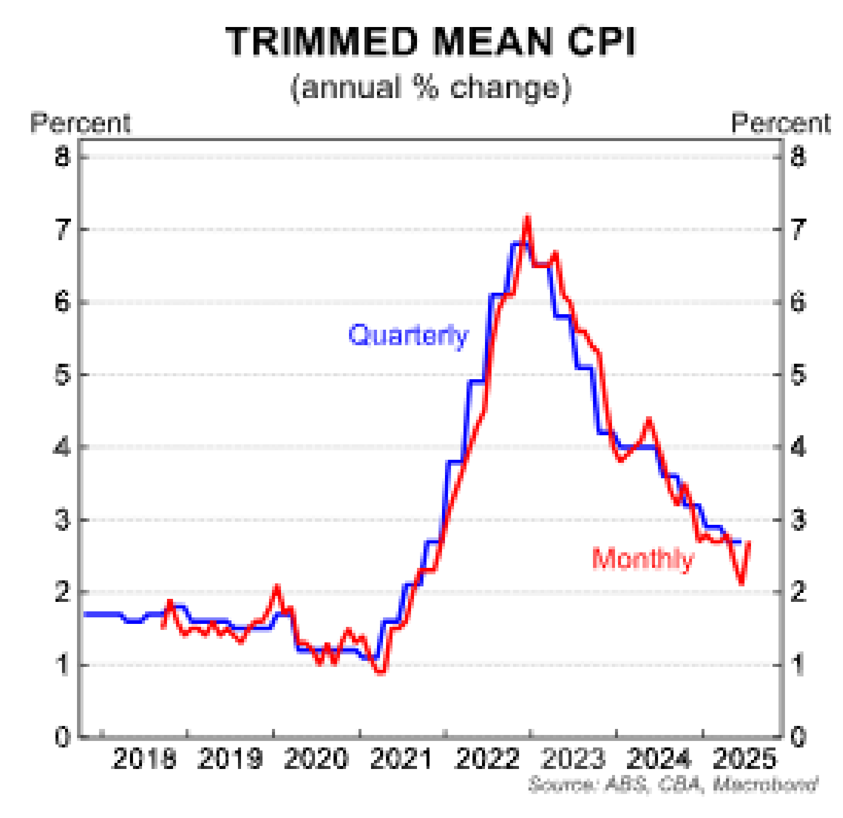
- The challenge for Australia's (and all nations) energy transition will be to deliver a low-emissions energy system that is both affordable and reliable.
- Research by the CommBank Sustainable Economics team shows that electricity supply in Australia has reduced its carbon intensity over the past 5 years – but with prices rising and reliability reducing, though these factors are not necessarily causal.
- Higher prices for gas, due to a lack of domestic supply, and the need to transition away from coal-fired power to renewables will continue to be challenging factors for Australia.



Source: CommBank Economics, 31 July 2025

Australia – Inflation trending lower

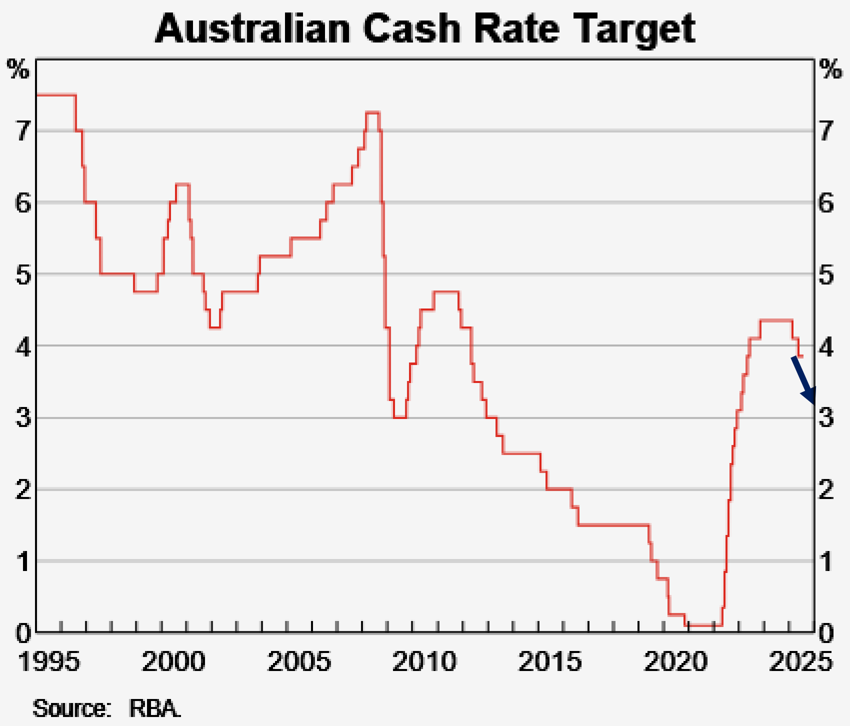
- After peaking at 7.8% in Q4 22, Australia's headline inflation rate has dropped to just 2.1% as at Q2 25.
- The all-important trimmed mean (underlying) inflation rate is 2.7% as at Q2 25.
- The monthly CPI jumped to 2.8%/yr in July – but this was largely due to timing issues with the electricity rebates - the annual trimmed mean remained at 2.7%/yr.
- Importantly, inflation by both measures is now firmly back inside the RBA's 2%-3% target range.
- The RBA is forecasting headline inflation at 3.0% at year-end 2025 (as the electricity rebates fall out), 2.9% year-end 2026 and 2.6% mid-2026.
- The underlying inflation rate is forecast at 2.6% year-end 2025 and all the way out to mid-2027, ie. slightly above the mind-point of the target range.



Source: CommBank Economics, 27 August 2025

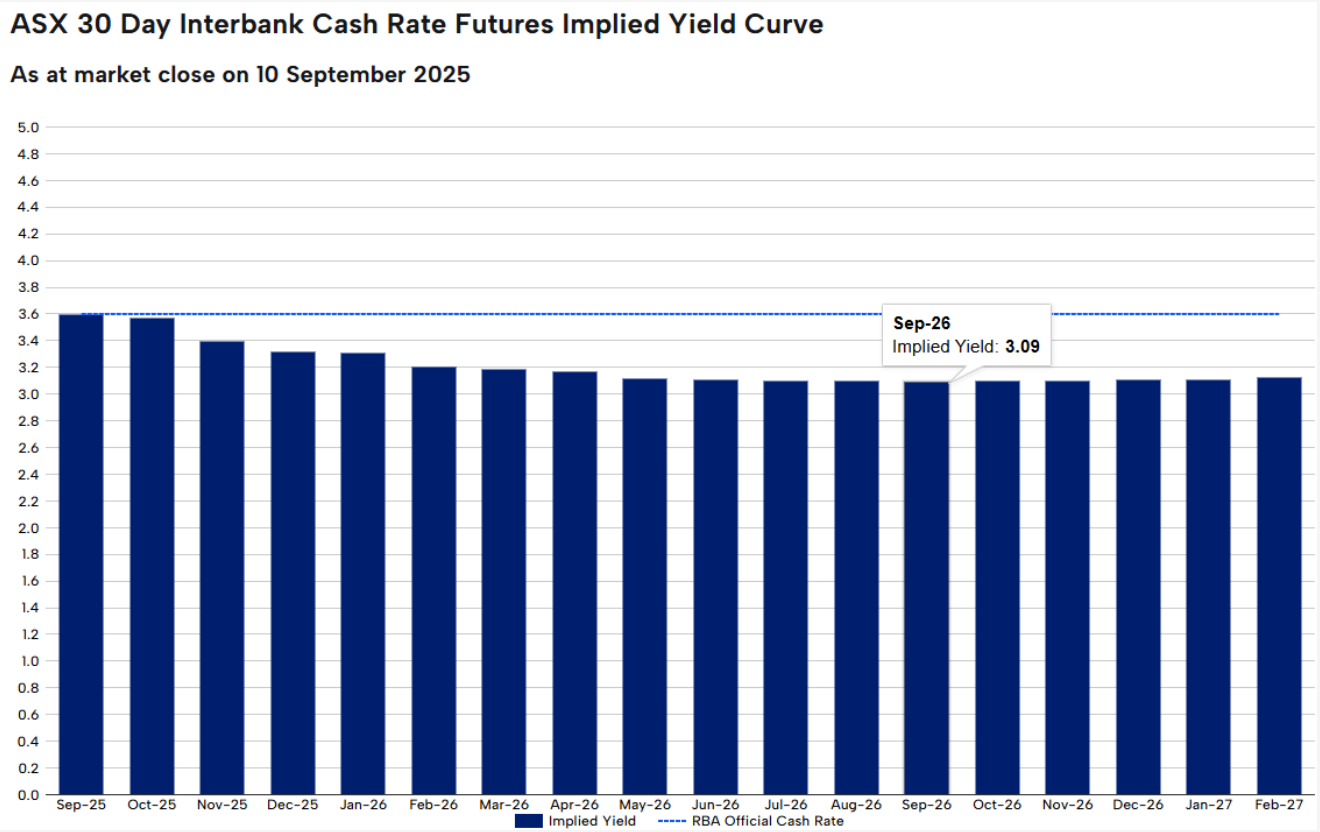
Australia – More interest rate cuts coming

- The RBA cut the cash rate by a further 25bp, to 3.6%, on 13 August 2025 – after the surprise ‘on hold’ decision in July.
- The RBA noted that “inflation has fallen substantially since the peak in 2022, as higher interest rates have been working to bring aggregate demand and potential supply closer towards balance. (RBA forecasts) suggest that underlying inflation will continue to moderate to around the midpoint of the 2%-3% range, with the cash rate assumed to follow a gradual easing path.”
- Importantly, the RBA is also of the view that a global ‘tariff war’ would be deflationary for Australia.
- Steady inflation and a softer labour market should see the RBA continue to ease policy in coming months.
- Expect to see two more 25bp rate cuts in this cycle (to 3.1%) – with a base case of November 2025 and February 2026.
- This will take monetary policy to a neutral setting.



Australia – Monetary policy to return to neutral

- The RBA and market estimates are that the neutral cash rate is in a range around 3.0%-3.5%.
- At the current 3.6% cash rate, monetary policy is still marginally restrictive.
- In a world where uncertainty has increased significantly and where Australian inflation is within the target range, it would make sense for the RBA to return monetary policy to a more neutral setting in coming months.
- Expect two more rate cuts, to 3.1%, over the remainder of 2025/early 2026.
- This is largely priced into markets.



Source: ASX Rate Tracker, 11 September 2025

Longer-Term developments – Focus on the six Ds

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1. *Demographics* – The ‘ageing’ of the baby-boomers, spending and wealth transfer.
2. *Decarbonisation* – Expensive, but critical.
3. *Defence* – Spending to increase on geopolitical uncertainties and spheres of influence.
4. *Debt* – Rise of government debt could lead to reduced services, increased taxes and/or increased instability in markets.
5. *Decoupling* – From China, significant disruption to global supply-chains.
6. *Digitisation* – The power of AI. Will drive the value of human expertise towards zero!

Important Information and Disclaimer

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