2. THE ECONOMY

- The NSW economy is gradually returning to normal following the significant disruptions primarily caused by the COVID-19 pandemic. For most of the last three years, the rising cost of living and higher interest rates have put pressure on households.
- Cost-of-living pressures have begun to ease, with inflation back within the Reserve Bank of Australia's (RBA) target range. Confidence that inflation would move sustainably towards their target has allowed the RBA to commence lowering interest rates.
- The unemployment and underemployment rates have stayed low by historical standards.
- Residential construction has been the slowest sector to normalise, given post-COVID population growth and the long lead times to build new dwellings. However, dwelling completions over the next four years are expected to outpace population growth.
- The United States of America's (US) tariff policies are expected to have modest direct implications for the NSW economy. However, their effect on business and consumer confidence over the next year or two is expected to slightly lower economic growth.
- While global developments always pose economic risks, unpredictable US policies and the potential for retaliatory actions by other countries are increasing uncertainty and the risks around economic forecasts.
- Overall, underlying economic fundamentals point to a pick-up in growth as cost-of-living pressures ease and the RBA lowers rates further. This should help keep the unemployment rate low.

Table 2.1: New South Wales economic performance and outlook[(a)]

	2023-24 Outcome	2024-25 Forecast	2025-26 Forecast	2026-27 Forecast	2027-28 Forecast	2028-29 Forecast
Real state final demand[(b)]	1.3	1¼ (¾)	2¼	2¼	2¼ (2½)	2½
Real gross state product	1.2	1¾ (¾)	1¾ (2½)	2¼	2(2¼)	2
Employment	2.1	2	1 (1½)	1¼ (1½)	1½	1¼
Unemployment rate[(c)]	3.9	4(4½)	4¼ (4½)	4¼	4	4
Sydney consumer price index	4.3	2½ (3)	3	2½	2½	2½
Wage price index	4.1	3¼ (3½)	3½ (3¼)	3(3¼)	3(3½)	3
Nominal gross state product	5.3	3¾ (3¼)	3¼ (5¼)	5 (4¼)	5 (4½)	5¼
Population[(d)]	1.7	1.3	1.1 (1.3)	1.1 (1.2)	1.1 (1.2)	1.1

(a) Forecasts are rounded to the nearest quarter point and are annual average per cent change, unless otherwise indicated. 2024-25 Half-Yearly Review forecasts in parentheses where different.
(b) Forecasts completed prior to publication of the March quarter 2025 National Accounts by the Australian Bureau of Statistics (ABS).
(c) June quarter, per cent.
(d) Per cent change through the year to 30 June. Forecasts rounded to nearest 0.1 percentage point.

Note: Forecasts finalised 12 May reflecting data up to 30 April.

Source: ABS and NSW Treasury

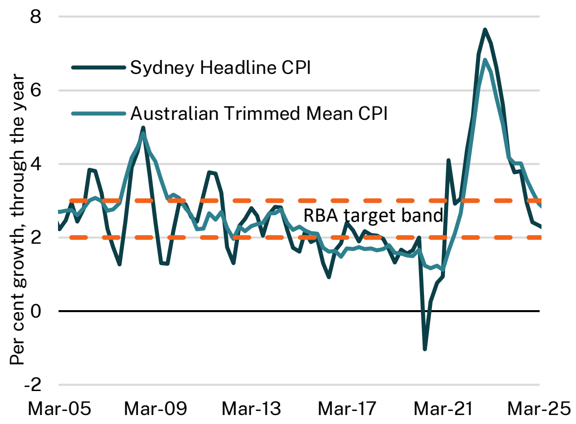
2.1 The New South Wales economy is on track to recover

Growth in New South Wales domestic spending has been subdued for most of the past three years, especially on a per capita basis, reflecting the rising cost of living and higher interest rates.

Cost-of-living pressures have eased over the past year. Inflation, as measured by the Sydney consumer price index (CPI), declined to 2.3 per cent over the year to the March quarter 2025, broadly in line with the RBA's inflation target. This is down from 3.8 per cent a year earlier. A similar decline in inflation has occurred nationally.

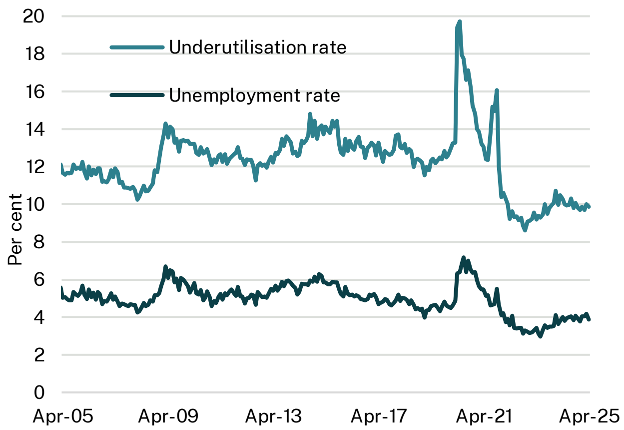
Government electricity rebates and lower fuel prices have helped to curb headline inflation. In the March quarter 2025, national trimmed mean inflation, at 2.9 per cent, also fell within the RBA's target range for the first time in three years (Chart 2.1). While progress on inflation has been supported by slower goods prices inflation for some time, services inflation (usually considered more 'sticky') is now also showing signs of deceleration.

Chart 2.1: Sydney headline and national trimmed mean CPI



Source: ABS, RBA and NSW Treasury

Chart 2.2: NSW unemployment and underutilisation rate



Source: ABS and NSW Treasury

Continued strength in the labour market

Lower inflation has occurred despite continued strength in the labour market, which has remained remarkably resilient and broadly consistent with full employment. Strong and sustained labour demand has underpinned solid employment growth, with trend employment rising by 2.4 per cent over the year to April 2025.

The supply of labour has been helped by an elevated participation rate, which has remained near its record high over most of the past year. This largely reflects an increase in the female participation rate to a record high. The NSW population has grown at 1.4 per cent through the year to the September quarter 2024, which is slightly above its long-run average growth. However, employment growth has slightly outpaced population growth, with the employment-to-population ratio rising modestly over the past year to a historically high rate of 63.8 per cent in April 2025.

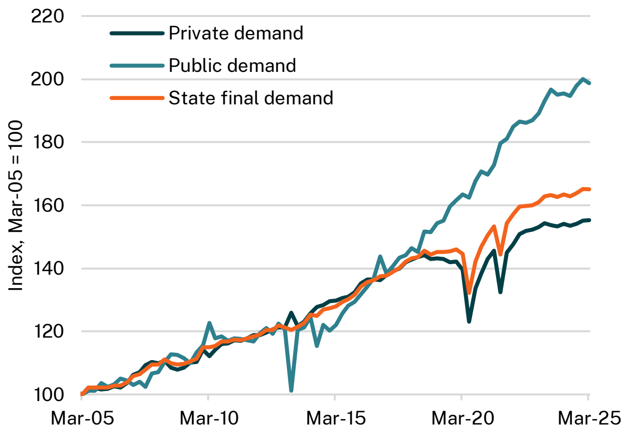
As labour supply has largely been absorbed by labour demand, the unemployment rate has remained steady at around 4.0 per cent. Broader measures of labour market slack have, if anything, pointed to some tightening in labour market conditions over the past year. Notably, the underutilisation rate has not only stayed well below pre-COVID levels, but it has declined from an average of 10.2 per cent in the first half of 2024 to 9.9 per cent as at April 2025 (Chart 2.2).

Public demand has helped smooth growth in the economy

Much of the recent strength in employment has been concentrated in the non-market sector, particularly in health and education, of which the public sector makes up a significant share. This reflects continued strong growth in public spending in these areas.

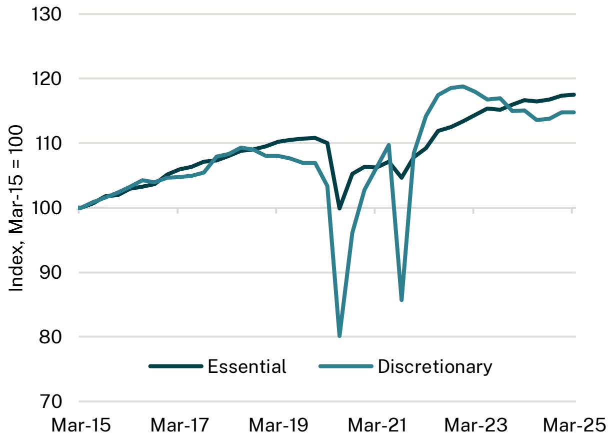
Alongside targeted investment in key areas such as the State's essential infrastructure program, public demand grew by 2.1 per cent over the first three quarters of 2024-25. This was despite a contraction in public demand in the March quarter 2025, reflecting a fall in both public consumption and investment. Over the last three quarters, public demand contributed more than 40 per cent to growth in total state final demand (compared to the pre-COVID historical average of under 25 per cent). This continues the strong contribution from public demand seen over the past five years (Chart 2.3).

Chart 2.3: NSW real state final demand



Source: ABS and NSW Treasury

Chart 2.4: NSW real discretionary and essential consumption



Source: ABS and NSW Treasury

Easing cost-of-living pressures are supporting a recovery in private demand

Private demand has been supported in 2024-25 by an easing of cost-of-living pressures, reflecting cuts to personal income tax and more moderate inflation. The resulting increase in real disposable household incomes has bolstered savings and helped to stabilise discretionary spending, which had previously been in steady decline. Spending on essential consumer goods and services has continued to increase at a modest pace (Chart 2.4).

Having declined by 0.5 per cent over the year to the June quarter 2024, real household consumption has increased by 1.0 per cent over the first three quarters of the 2024-25 financial year. Much of this strength occurred in the second half of 2024, with large retail sales events and seller discounting bringing forward discretionary spending from the early part of 2025. Adverse weather conditions may have also slightly curtailed consumer spending in the early part of 2025.

For now, the pace of growth in consumer spending remains subdued relative to history, particularly on a per capita basis. While consumer sentiment improved earlier in the year with expectations of interest rates cuts, it remains below historical averages. Sentiment has dipped slightly in more recent months in response to uncertainty over the global economy.

The renewable energy transition is helping business investment

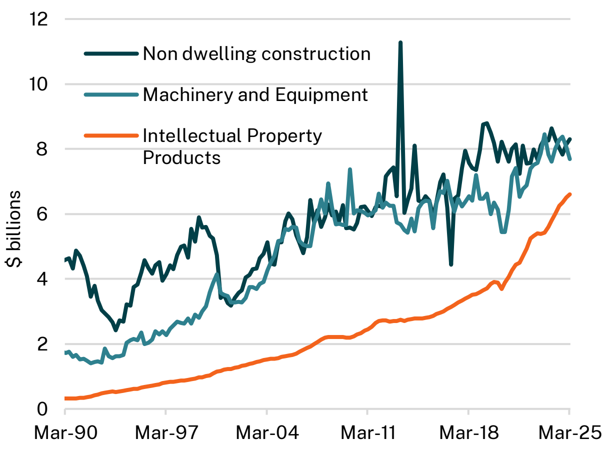
Businesses have faced tight capacity in recent years, providing a catalyst for higher rates of business investment. However, after posting solid growth in 2023–24, business investment rose by a relatively subdued 1.0 per cent through the year to the March quarter 2025.

Investment in intellectual property products, such as computer software, has been a key driver of growth and has accounted for a steadily increasing share of the economy in recent years. In contrast, investment in new machinery and equipment fell over the year, down by 3.3 per cent (Chart 2.5).

Non-dwelling construction was broadly flat through the year to March quarter 2025, which likely reflects persistently high input costs, despite recent signs that some construction-related input costs are beginning to stabilise.

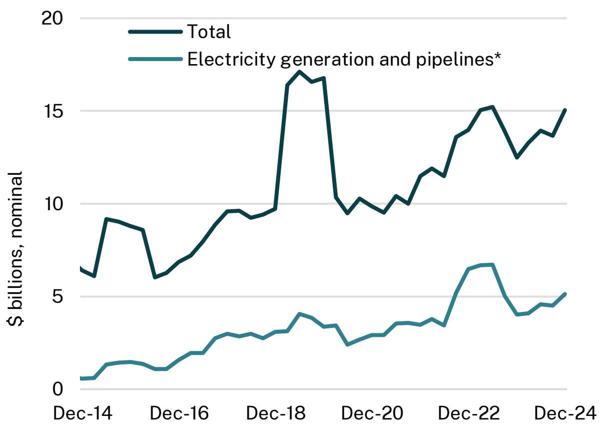
Against this, renewables remain a bright spot. According to ABS data, investment in renewable energy construction rose by 4.7 per cent in 2023–24. New South Wales has recorded a solid increase in private engineering commencements in electricity and utilities, much of which is related to the transformation of the State's energy system (Chart 2.6). The NSW Government is assisting the transformation through Renewable Energy Zones.

Chart 2.5: NSW real business investment



Source: ABS and NSW Treasury

Chart 2.6: NSW private engineering work commenced



Source: ABS and NSW Treasury

**Includes electricity generation, transmission and distribution*

Residential construction activity has been the slowest sector to normalise

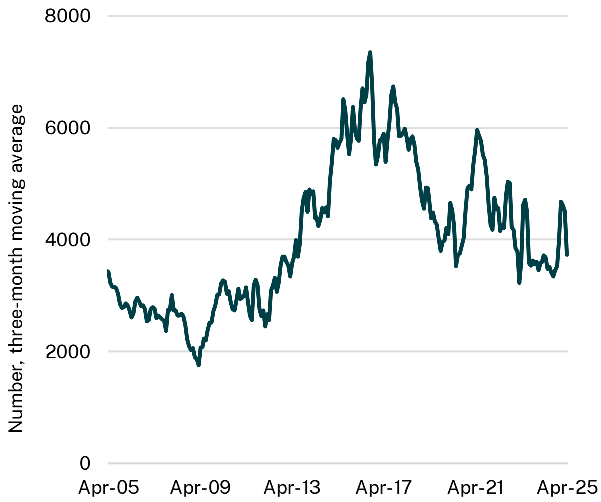
Following the COVID-19 pandemic, significant increases in construction input prices due to global supply chain issues, along with competition for resources from public infrastructure investment, placed pressure on the residential sector, leading to a significant surge in construction prices and increasing insolvencies. In addition, the increase in interest rates by the RBA adversely affected the profitability of developments. The re-opening of Australia's international border following the pandemic was an additional factor interacting with these pressures.

As a result of these factors, residential construction activity has been slower to pick up compared to other sectors. Some of the factors holding back dwelling investment showed signs of easing in the second half of 2024. Notably, construction cost inflation eased while capacity utilisation in the construction sector fell to its historical average level. This allowed residential projects already in the pipeline to move closer to completion. Dwelling approvals rose in the March quarter 2025 to an almost two-year high. However, approvals have fallen back in recent months as elevated construction costs continue to impact the profitability of apartment projects (Chart 2.7).

The same cyclical forces that restrained dwelling construction also affected the established dwelling market. Strong population growth against the backdrop of constrained housing supply has worked to support prices. Conversely, high interest rates have worsened affordability for new borrowers, contributing to a modest downturn in prices in late 2024.

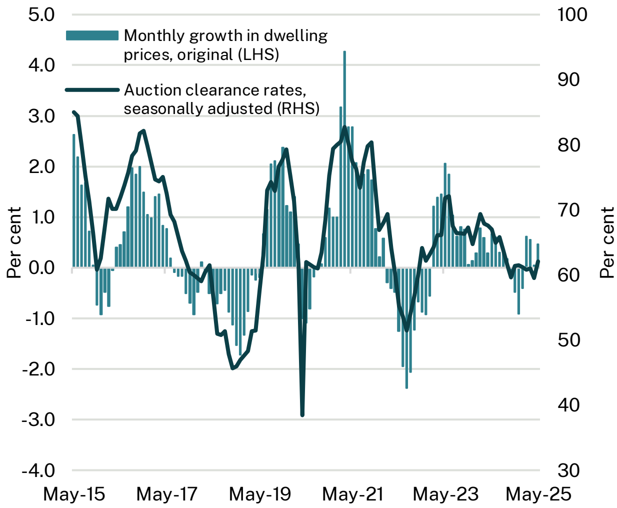
Sydney dwelling prices have risen modestly in the months since the commencement of the cash rate easing cycle in February. Interest rate cuts have supported buyer sentiment, with auction clearance rates rising in May to a level consistent with modest price growth (Chart 2.8). Recent dwelling price growth has been strongest in those segments that are typically more rate sensitive, such as detached housing, reflecting increased borrowing capacity as rates decline. In contrast, price growth in less rate-sensitive segments has been slower to recover.

Chart 2.7: NSW residential construction approvals



Source: ABS and NSW Treasury

Chart 2.8: NSW auction clearance rates and monthly growth in dwelling prices



Source: Cotality and NSW Treasury

Net exports have supported aggregate growth

Growth in gross state product (GSP) is expected to have outpaced the subdued increase in state final demand (SFD). GSP is estimated to grow by 1¾ per cent in 2024-25, compared to growth of 1¼ for SFD.

NSW GSP growth has been supported by a strong rise in exports, particularly through the earlier part of 2024-25, underpinned by increases in both rural and resource commodities. The lift in rural exports was driven by higher shipments of vegetables, fruits, oilseeds and chickpeas. This was supported by favourable weather, increased domestic production, and strong overseas demand, particularly following a temporary removal of Indian tariffs on chickpea imports. Coal exports also rose sharply in early 2024-25, as China boosted purchases ahead of winter due to lower hydropower generation. The positive impact to growth from these factors are expected to be temporary and somewhat unwound in the March quarter 2025.

Interest rate cuts are now supporting activity, with more rate cuts expected

Cost-of-living pressures have been further helped by the recent easing in monetary policy. The RBA has reduced interest rates twice since February, from a peak of 4.35 per cent to the current 3.85 per cent, a slightly earlier decline than expected at the time of the 2024-25 Half-Yearly Review. A NSW borrower who took out an average-sized new mortgage (around $810,000 in the December quarter 2024) would have seen their monthly repayments on a 30-year loan fall by a little under $260 per month, or around $3,100 a year.

Consistent with market expectations at the time the forecasts were finalised, two further rate cuts are expected over the remainder of 2025, with one further rate cut in the first half of 2026, which would bring the cash rate to 3.1 per cent. However, the RBA has noted that it will be attentive to the data and the evolving assessment of risks to guide its decisions. The profile for the interest rate assumption is broadly in line with the RBA's assumptions at the time of the May 2025 Statement on Monetary Policy.

2.2 Outlook for the New South Wales economy

Uncertainty around the global backdrop is likely to weigh on the domestic economy

Recent events have made the global environment more challenging for the NSW economy. In addition to broader geopolitical unrest, recent developments in US trade policy have been a standout as US President Trump followed through on his rhetoric leading up to the Presidential election with a range of announcements levying tariffs on almost all countries exporting to the US.

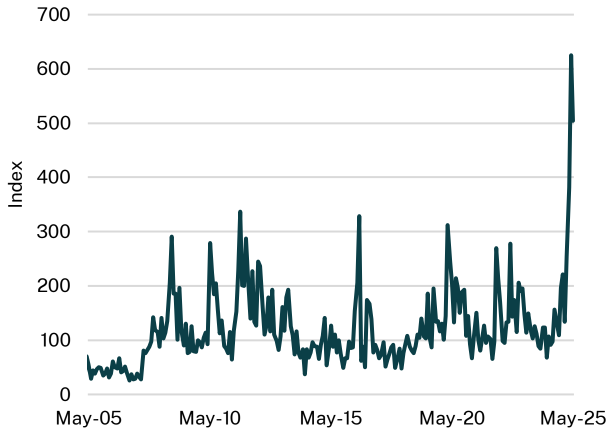
In particular, financial markets were initially thrown into turmoil following the "Liberation Day" tariff announcements of a minimum 10 per cent tariff on all goods imported (and a much higher tariff rate on imports from China) into the US economy. The resulting sharp spike in global policy uncertainty (Chart 2.9) coincided with share markets falling abruptly while the Australian dollar fell to below US60 cents, as these policies were seen as having a marked impact on global trade and growth.

In response, the International Monetary Fund (IMF) downgraded its expectations for global growth in 2025 and 2026 by a cumulative 0.8 percentage points from its forecast in January. The IMF expects the global economy to grow by 2.8 per cent in 2025 and 3.0 per cent in 2026. This is significantly below the average growth rate of 3.7 per cent in the two decades prior to COVID-19.

The subsequent pause in the implementation of higher tariff rates alongside announcements of a trade deal between the US and the UK, and progress in trade negotiations between the US and China, have seen financial markets recover. Notwithstanding this, uncertainty around the global policy outlook remains unusually elevated.

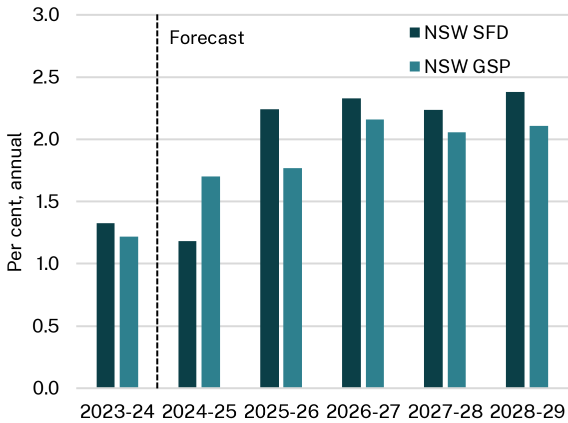
Several institutions, including the World Bank and the RBA, have followed the IMF's lead and subsequently downgraded the outlook for growth. NSW Treasury has undertaken modelling of the impacts on the NSW economy, detailed in Box 2.1.

Chart 2.9: Economic policy uncertainty index (Australia)



Index based on the degree of news coverage of policy-related economic uncertainty.
Source: 'Measuring Economic Policy Uncertainty' by Scott Baker, Nicholas Bloom and Steven J. Davis at www.PolicyUncertainty.com

Chart 2.10: NSW real economic growth 2023-24 to 2028-29



Source: ABS and NSW Treasury

Box 2.1: US tariff impacts on the NSW economy

There has been an increase in protectionist trade policies globally in recent years. Trade tensions present uncertainty and volatility for the global economy.

Tariffs increase the cost of imported goods and services. This can reduce demand for foreign exports. Trade barriers, including tariffs, can have negative flow-on effects. These include lower business and consumer confidence, and higher inflation.

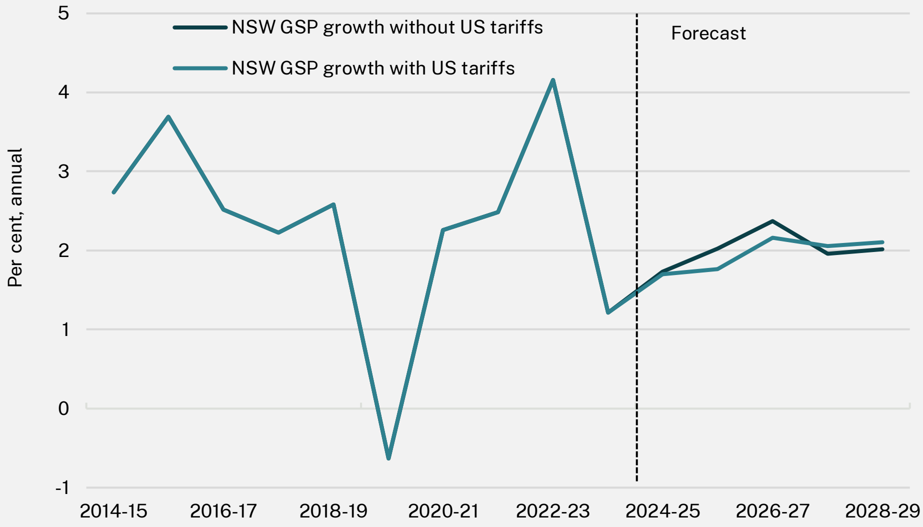
The direct impact of announced US tariffs on New South Wales is expected to be modest. In 2023-24, goods exports to the US represented 0.6 per cent of NSW nominal GSP. If tariffs result in reduced demand from the US, NSW exporters will likely find alternative markets for selling their products.

The indirect effects of these tariffs are likely to be larger than the direct effects. In particular, frequent changes to the scope and extent of tariffs are contributing to increased global uncertainty. This was reflected in the RBA's recent forecast downgrades to Australian gross domestic product growth.

NSW Treasury expects that the resulting delay to investment and consumer decisions will lead to a small decrease of around ½ a per cent from the level of GSP over two years, with more than two thirds of that coming from weaker business investment (Chart 2.11). The remainder stems from consumption, although with some offset from lower imports.

For now, these shocks are expected to be temporary and to unwind somewhat as either the political situation stabilises or consumers and businesses adjust to this environment. As such, only minimal effects on NSW GSP and employment are expected in the medium term.

Chart 2.11: Impact of US tariffs on NSW real GSP growth



Source: ABS and NSW Treasury

Fundamentals remain supportive of a gradual improvement in the NSW economy

Notwithstanding the risks from global uncertainty, the outlook remains consistent with a gradual pick-up in the pace of growth in the NSW economy.

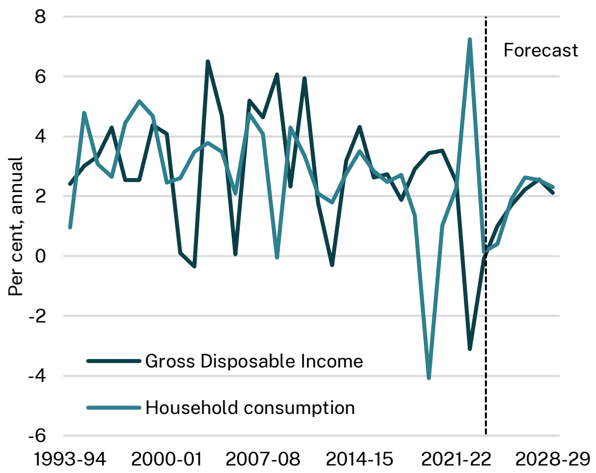
With cost-of-living pressures likely to ease further as the RBA continues to lower interest rates, real wages increasing, and conditions in the labour market remaining solid, the NSW economy is well positioned for a lift in economic growth. Shifts in global supply chains due to US tariffs may also present new opportunities, potentially presenting new markets for NSW exporters, particularly in the Asia-Pacific region. Domestic spending is expected to pick up, with SFD expected to grow by 2¼ per cent in 2025-26. However, weaker exports will mean this does not fully translate into stronger GSP. GSP growth in 2025-26 is expected to be 1¾ per cent, broadly in line with growth in 2024-25 (Chart 2.10).

Central to the outlook is an expected rotation of growth from the public sector to the private sector. This will be aided by an expected slower pace of growth in public demand as governments seek to improve their fiscal positions. Consumer spending is expected to lead the recovery in private sector activity, though this will take time as elevated policy uncertainty weighs further on a still cautious consumer in the next few months. As 2025 progresses, household consumption is expected to gradually improve as interest rate cuts ease household financial burdens, particularly for mortgage holders. In conjunction with further tax cuts, extended energy rebates, steady employment growth, and rising real incomes, these are expected to strengthen household disposable income and support consumption growth throughout the forecast period (Chart 2.12).

Business investment is also expected to be supported by positive fundamentals. Strong business balance sheets, a tight labour market and elevated capacity utilisation will provide an incentive for businesses to keep the overall level of business investment elevated, particularly as consumer spending recovers and concerns over the global and domestic growth outlook fade.

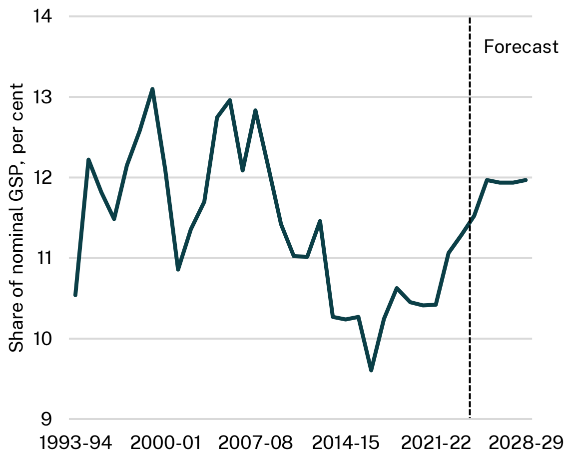
Recent trends are indicating a shift in the capital expenditure pipeline from the public to the private sector, particularly within engineering construction. The pipeline of engineering construction activity in the private sector is being led by industries such as electricity utilities and heavy industry. This uplift is being supported by a continued increase in renewables investment, underpinned by the ongoing transition to renewable energy. NSW's strong focus on the renewable energy and technology sectors may position it to attract investment as the global economy adjusts to these changes. Overall, business investment is expected to grow broadly in line with its historical average over the next four years. This would result in its share of GSP returning to its average level prior to the Global Financial Crisis (Chart 2.13).

Chart 2.12: NSW real household income and consumption growth



Source: ABS and NSW Treasury

Chart 2.13: NSW business investment



Source: ABS and NSW Treasury

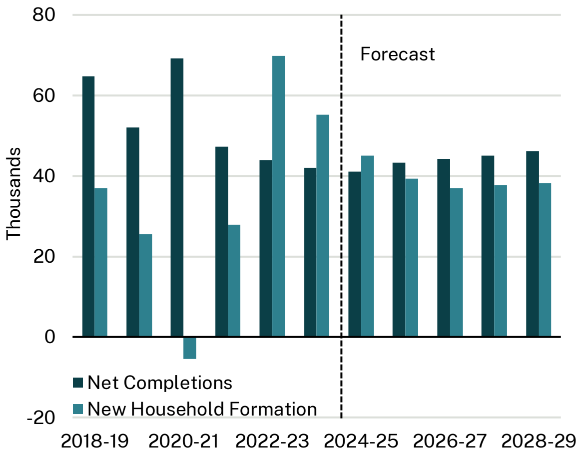
Housing completions will outpace underlying demand for housing over the forecast period, but affordability remains stretched

New dwelling investment is forecast to rise as the cyclical headwinds that have weighed on the sector subside to an extent. Lower interest rates are expected to support greater development feasibility via reduced financing costs and dwelling price appreciation. In addition, inflation in the price of construction materials has fallen and the availability of suitable labour is beginning to improve. Over the forecast period, both labour and raw material availability are expected to further benefit from the unwinding of the large public sector construction pipeline, increasing the capacity for residential construction, particularly in the higher-density segment.

Despite this, low levels of dwelling approvals in recent years mean that a significant uplift in dwelling completions will likely take several years to eventuate. Currently, the lead times between approvals and completions for housing is two years, while for apartments it averages around three years. Recent changes in planning regulations designed to lift approvals will further encourage housing completions. Around 240,000 dwelling completions are forecast for New South Wales over the five years to the end of 2028-29 (Chart 2.14).

At the same time, while lower interest rates are expected to help mortgagees, housing affordability is expected to remain constrained compared to its historical level (Chart 2.15). Lower interest rates and improved market sentiment are expected to see growth in Sydney dwelling prices pick up in the near term. The Westpac-Melbourne Institute Time to Buy a Dwelling Index has trended upwards since mid-2024 amid increased optimism around family finances and future rate cuts. This is expected to translate into increased buyer demand. From late 2026, dwelling prices are projected to grow broadly in line with household incomes, once interest rates have stabilised at long-run neutral levels.

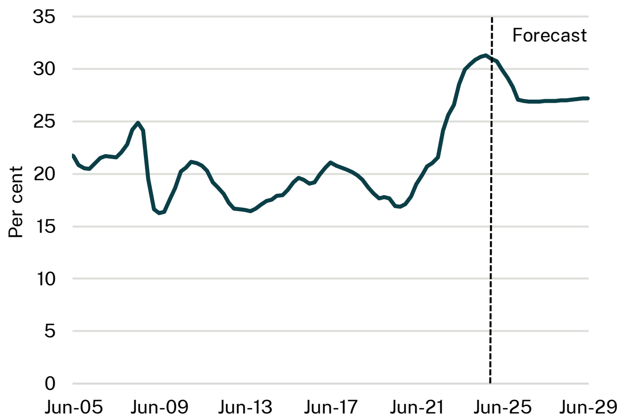
Chart 2.14: Net completions vs underlying demand for housing



Source: ABS and NSW Treasury

Note: New household formation is the change in the year-average population divided by an assumed average household size of 2.5. Net completions forecasts use twenty-year average demolition rates.

Chart 2.15: NSW mortgage payments as a share of household income

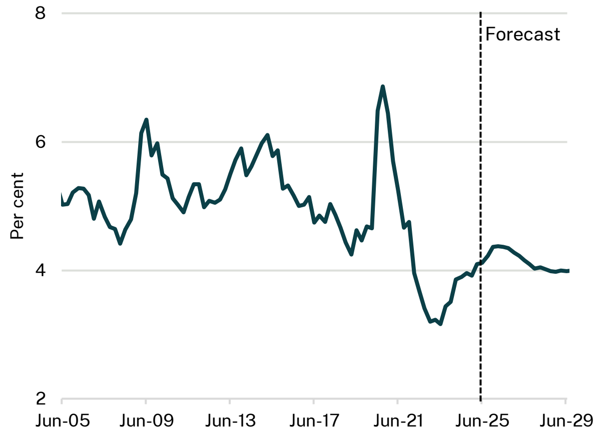


Source: ABS, RBA, Cotality, HILDA and NSW Treasury

Unemployment will remain low by historical standards

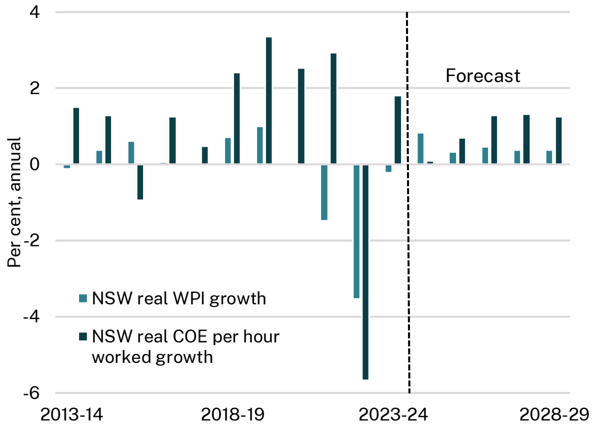
The expected strengthening in economic growth momentum should see the labour market remain resilient in the face of the uncertain global environment. Nevertheless, a slowing in non-market sector employment growth is expected to drive a softening in aggregate employment. This will be accentuated by business efforts to drive a pick-up in market sector productivity following the weakness of recent years which should see the unemployment rate lift modestly in the period ahead. Despite this, the expected peak in the unemployment rate of around 4.4 per cent remains very low by historical standards (Chart 2.16).

Chart 2.16: NSW unemployment rate forecasts



Source: ABS and NSW Treasury

Chart 2.17: Growth in NSW real wages



Source: ABS and NSW Treasury

Continued tightness in the labour market should see wages growth remain somewhat elevated in 2025-26, albeit down from the pace seen in the past two years. The NSW wage price index (WPI) is forecast to grow by 3½ per cent in 2025-26 before slowing to around 3 per cent in 2026-27.

The forecast for WPI is above our base case forecast for headline inflation, which is expected to remain within the RBA's 2–3 per cent target range over the remainder of 2025. As electricity rebates expire, headline inflation is expected to temporarily rise above the target range in the first half of 2026. Broader inflationary pressures are better reflected in underlying inflation, which at the national level is expected to remain sustainably within the RBA's target band and continue easing, reaching the mid-point of the range by early 2026.

The combination of solid nominal wages growth, lower inflation within the RBA's target band and a pick-up in productivity growth is expected to result in continued real wages growth (Chart 2.17). Over the five years to June 2029 real wages, as measured by the average compensation of employees, are expected to grow by an average of 0.6 per cent per year. This compares to an estimated -0.1 per cent over the five years to June 2025. This solid growth in real wages is key to ensuring self-sustaining growth in the economy over the forecast period.

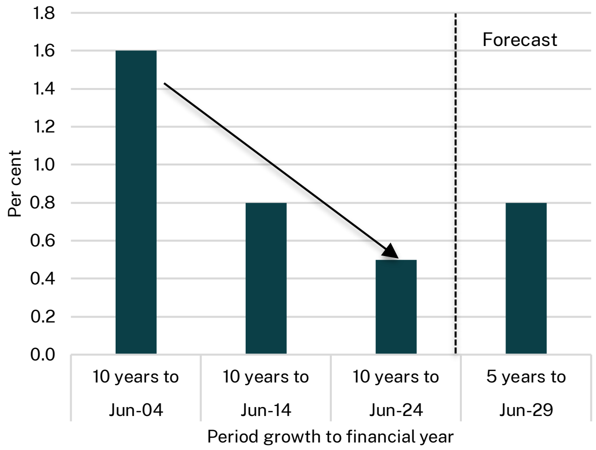
2.3 Productivity as a driver of growth and living standards

Unlocking productivity growth is vital as the NSW economy evolves

Productivity growth is a key determinant of living standards and an important driver of economic growth in the long term.

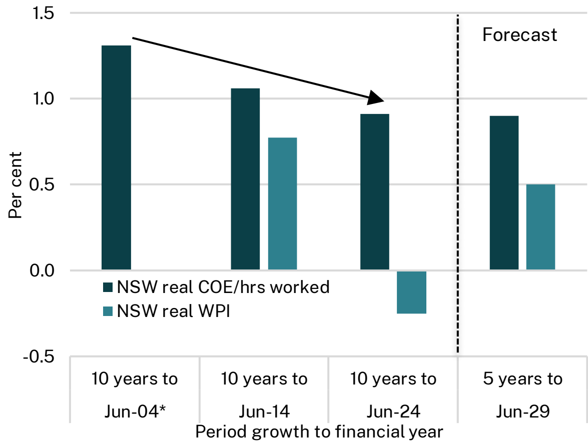
Box 2.2 outlines recent developments in productivity. Reflecting this, the current expectation is that long-run productivity growth will reflect the 20-year Australian average of around 0.8 per cent (Chart 2.18). When combined with population growth of around 1.1 per cent, long-run potential economic growth in New South Wales is likely to settle around 1.9 per cent.

Chart 2.18: NSW productivity growth



Source: ABS and NSW Treasury

Chart 2.19: NSW real wages growth



Source: ABS and NSW Treasury

**WPI data is not available*

Over the long run, real wages are expected to increase in line with productivity growth (Chart 2.19). To be consistent with the RBA's inflation target, nominal employee incomes are expected to grow over the long run at around 3.3 per cent (2.5 per cent inflation plus 0.8 per cent average productivity growth).

Lifting productivity growth is the key to lifting real household incomes and economic growth. Most productivity growth is generated by private sector decisions. Nevertheless, governments can encourage productivity growth by improving the efficiency of the public sector, by setting appropriate regulatory environments, and by helping to ensure that workers are equipped with the skills, technology and infrastructure to do their jobs more efficiently.

To boost productivity and support long-term economic growth, the NSW Government is investing in infrastructure, education, innovation, and regulatory reform. The State has also established the Investment Delivery Authority to help increase productivity growth and investment in New South Wales.

Box 2.2: Recent developments in productivity and impact on forecast growth

Productivity growth has slowed in domestic and global economies

Labour productivity growth has been weak since the onset of COVID-19, averaging just 0.4 per cent per year in New South Wales in the past five years.

This weakness was evident even prior to COVID-19. Over the 10 years to 2023-24 productivity growth in New South Wales averaged 0.5 per cent per year. This compares to an average of 0.8 per cent per year in the 10 years to 2013-14 and 1.6 per cent over the decade to 2003-04.

This declining trend in productivity growth has been observed both nationally and globally (see Table 2.2).

Table 2.2: Average productivity growth in Australia and advanced economies[a]

(CAGR)	1994 to 2004	2004 to 2014	2014 to 2024
NSW	1.6	0.8	0.5
AUS	2.2	1.2	0.5
Advanced economies[b]	1.9	1.0	0.9

(a) Growth is for fiscal years for New South Wales and Australia, and for calendar years for advanced economies.
(b) Advanced economies include Australia, USA, Euro Area, Canada, Japan, UK and NZ.

Source: ABS, Long term Productivity Database, International Monetary Fund and NSW Treasury

Given productivity growth was weak even before COVID-19, it is unlikely cyclical factors alone are to blame. Work by the RBA indicates that the slowing in productivity growth in Australia primarily reflects structural factors, including:

- increasing demand for non-market services (and persistent mismeasurement of non-market sector output)
- a lack of capital deepening
- declining economic dynamism
- increasing regulatory barriers
- slowing human capital accumulation
- less trade integration.

This suggests that in the absence of meaningful reforms or a major technological breakthrough, low productivity growth will continue.

Over the next 2-3 years, productivity growth should pick up as the cyclical factors that have accentuated the trend decline fade.

However, it is expected that this will still leave productivity growth well below the level of earlier decades. The most recent 20-year average for Australia suggests this will be around 0.8 per cent.

The NSW Government can make meaningful changes to the structural barriers to productivity with investments in education and skills, more effective regulatory regimes, and efficient rebuilding of essential non-market services.

2.4 Key risks to the outlook

Risks remain unusually elevated

Uncertainty around the economic outlook remains unusually elevated.

Relative to the baseline forecasts, there is still a downside risk from tariffs. Counter to this, the potential for greater policy stimulus in China to combat against the impacts of a US-China trade war could see an unexpected lift in demand for NSW exports, especially in markets where tariffs on other countries' production make Australian exporters more competitive.

Additionally, another risk with upside potential is if the current policy uncertainty in the US leads to either a lower global cost of capital (as investment falls in the US), or Australia becoming a more desirable destination for foreign investors. Both outcomes would lead to a boost in onshore investment which could also support productivity over the forecast period. This risk is explored in Appendix F Economic *s*cenario analysis.

The housing market remains a notable source of risk to the outlook, in either direction. While dwelling prices have steadily recovered after falling for most of the second half of 2024, affordability challenges are still constraining buyers, amid slowing approvals for residential dwellings. On the upside, easing monetary policy to support the economy could improve buyer sentiment and support price growth, with positive spillovers to household consumption and dwelling investments.

There are upside inflationary risks that not only stem from the fragmentation of global supply chains and inefficiencies generated from protectionist policies, but also ongoing conflicts in the Middle East and Ukraine. Domestically, the continued strength in nominal wages growth over the coming year poses a potential upside risk to inflation if productivity fails to lift as quickly as expected.