Australia Economic Outlook

Q2 2026

July 2026

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KPMG Australia

Executive summary

The easing of the conflict in the Middle East through the recent signing of a Memorandum of Understanding between the US and Iran has reduced, but not eliminated, one of the most significant risks facing the world economy so far in 2026.

The escalation of the Iran conflict earlier in the year drove a sharp spike in global oil prices, with spot prices rising above US$100 per barrel at their peak. Although prices have since unwound from their heights as prospects for a peace agreement have improved, higher oil prices continue to feed through to higher energy, transport and input costs.

Domestically, inflation has proven more persistent than expected even prior to the commencement of this current conflict, prompting the RBA to lift the cash rate three times in early 2026. These cash rate increases have materially tightened financial conditions, with higher borrowing costs weighing on household cash flows, credit demand and business investment. However, in the June monetary policy meeting, the RBA held the cash rate at 4.35%, reflecting a desire to assess the cumulative impact of earlier tightening and evolving global uncertainties.

Economic activity slowed sharply in the March quarter 2026, with GDP growing by a modest 0.3% in the first three months of the year, down from 0.9% the December quarter 2025. Household consumption remains constrained by cost-of-living pressures and higher interest rates, while business conditions have deteriorated alongside rising uncertainty. This is compounded by a fragile underlying economy with weak productivity growth and softening GDP per capita.

The labour market is also beginning to ease. Employment growth has slowed, unemployment has edged higher, and forward indicators such as job advertisements suggest weaker demand ahead.

While wage growth remains contained overall, recent policy decisions – particularly the increase in minimum and award wages – are likely to add to cost pressures for businesses already experiencing margin compression.

Looking ahead, it will take time for inflation to return sustainably to target, given lingering cost pressures and the gradual pass-through of earlier shocks. Although fuel prices have been partially cushioned by temporary government support measures, limiting the immediate pass-through to headline inflation, the earlier surge in other important inputs, such as fertiliser prices in particular, has yet to be fully reflected in food prices.

Against this backdrop, while the RBA has held rates steady at its latest monetary policy meeting, the outlook for inflation suggests that further policy tightening cannot be ruled out. At this stage, we see the probability of another increase being very high.

Economic activity is expected to remain weak through 2026, with weak consumption acting as the primary drag in line with weak confidence and high interest rates. This presents a challenging trade-off for the RBA, as persistent inflation pressures coexist with a clear slowdown in economic activity. However, central banks have historically dealt with similar macroeconomic circumstances in periods of stagflation, where contractionary monetary policy settings where still employed in order to bring inflation backdown to target levels.

Weaker global economic activity is also expected to weigh on Australia's growth outlook. Commodity prices have remained relatively resilient to date, but the outlook is increasingly uncertain as global growth moderates. Nevertheless, the ongoing AI-driven investment cycle is providing an important offset to weaker global conditions via supporting demand for key commodity inputs and sustaining investment activity.

KEY FORECASTS	2025 (a)	2026 (f)	2027 (f)	2028 (f)
Real GDP				
Average annual growth	2.0%	1.8%	1.4%	1.8%
Year ended growth	2.5%	1.2%	1.6%	1.9%
Unemployment rate	4.3%	4.4%	4.7%	4.8%
Inflation				
Headline CPI	3.7%	4.0%	3.0%	2.7%
Core CPI	3.4%	3.0%	3.1%	2.8%
RBA cash rate	3.60%	4.60%	4.35%	4.35%
AUD/USD	0.67	0.71	0.71	0.71

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Global landscape

Global conditions

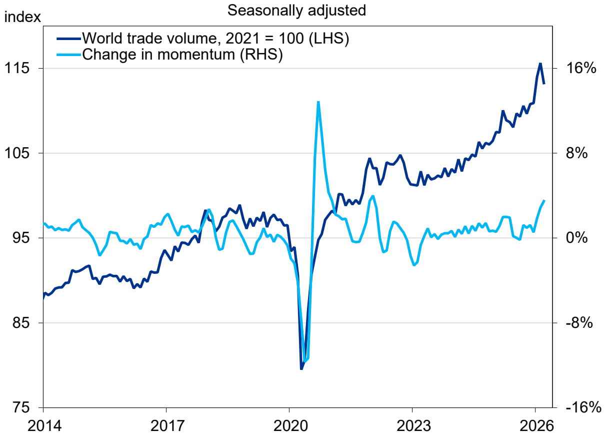
Recent data, though too early to fully capture the Iran conflict's impact on the global economy, points to resilient activity increasingly supported by strong AI investment. While some near-term disruptions have arisen, progress toward a peace deal suggests we can more confidently look through this as a temporary phase.

Recent data showed that global growth in the March quarter remained solid. Growth was supported by positive momentum, with economic activity towards the end of 2025 reasonably robust, alongside continued growth in AI-related demand.

Prior to the outbreak of the Iran conflict, household positions were generally improving and financial conditions were supportive, with expectations of further monetary policy easing.

Investment in advanced economies, particularly in the United States, has strengthened in line with the AI boom, driven by increased spending on new data centre capacity and expanding demand for electronics. This has also fuelled a boom in industrial production in several Asian economies, including Taiwan and South Korea, which specialise in advanced semiconductor manufacturing.

FIGURE 1
World Trade Volume
Seasonally adjusted



Source: CPB, Haver, KPMG

AI-induced demand for electronics has supported trade activity.

According to data from the World Trade Monitor, global trade volumes increased 0.7% in the March quarter to be up 3.5% through the year. This was the fastest pace of annual growth since the start of 2022. Moreover, momentum has been building, despite unresolved trade policy uncertainty.

Much of this benefit has been concentrated in advanced semiconductor manufacturing. During the March quarter, Taiwan recorded an astonishing 35.3% annual rise in exports.

Furthermore, the export price index accelerated for the eighth consecutive month in April, to be up 18.0% through the year, amplifying the return of higher trade volumes.

This extraordinary performance of the external sector has also been mirrored in South Korea, Singapore, and to a lesser extent, Japan and China.

However, in the background of this AI boom there remains some uncertainty surrounding the state of US tariffs, after the US Supreme Court ruled in February to strike down the baseline tariffs the US had imposed on its trading partners.

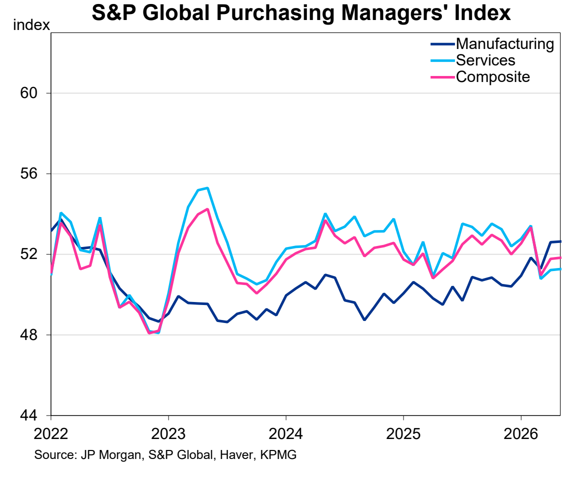
US President Donald Trump visited Beijing in May, the first visit by a US President since his previous trip in 2017. The visit yielded limited concrete deals but still reflected a positive shift in US–China relations. China's President Xi Jinping said both leaders agreed to build a 'constructive, strategically stable relationship', according to a Chinese foreign ministry statement, marking a 'new positioning' of ties.

No deal was made on extending the trade truce, which is due to expire later in the year, although both nations agreed to establish an investment board and a trade board, which would resolve concerns over market access and expand trade 'under a reciprocal tariff-reduction framework'.

Higher-frequency data suggest that global production activity declined at the onset of the Iran conflict but has since recovered.

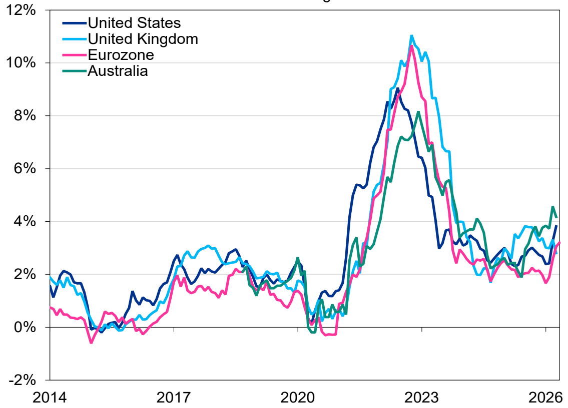
The Global Composite PMI Output Index dropped to an 11-month low of 51.0pts in March, before recovering to 51.8pts by May. Nonetheless, the index remains in expansionary territory, having done so for the last 40 months.

FIGURE 2
S&P Global Purchasing Managers' Index



Source: JP Morgan, S&P Global, Haver, KPMG

FIGURE 3
Inflation in Selected Advanced Economies
Year-ended growth



Source: BLS, ONS, Eurostat, ABS, Haver, KPMG *Aust. prior to Apr 2025 is Monthly CPI Indicator

Inflation has already increased sharply, reflecting the first-round impacts of the oil supply shock.

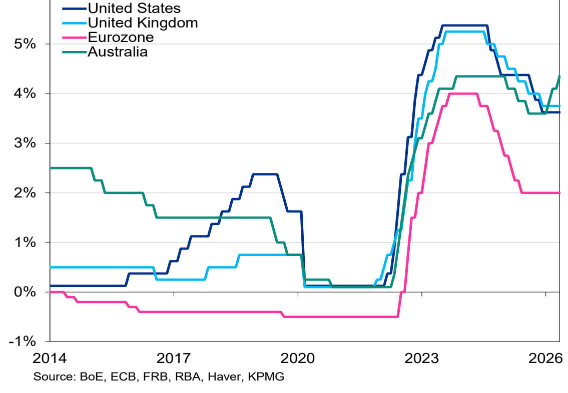
Prior to the outbreak of conflict in Iran, global oil prices had been on a sustained downward trend. However, the closure of the Strait of Hormuz has seen a significant shock to the supply of oil, sending the average spot price above US$100/bbl in both April and May.

This initial impact can already be seen in global headline inflation, which has accelerated sharply in response to higher fuel costs. Part of this inflation jump has been cushioned by government intervention in some nations, where fuel excises have been temporarily lowered and strategic fuel reserves have been supporting local consumption.

With the end of the conflict now in sight, it is looking likely that the worst of the global inflation shock is behind us, though it will take time for current inflationary pressures to unwind. However, secondary cost pass-through effects are still working their way through the broader system – particularly into higher food prices via higher fertiliser costs.

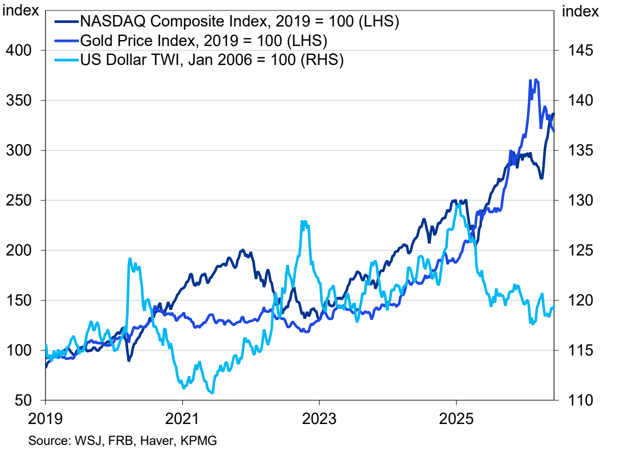
The risk of entrenched follow-on effects, such as persistently higher inflation expectations and a wage–price spiral, appear limited. While medium-term inflation expectations have moved upwards, they have not become significantly destabilised, allowing most central banks room to pause and 'look through' the supply side impacts so far.

FIGURE 4
Policy Rates in Selected Advanced Economies
End of period



Source: BoE, ECB, FRB, RBA, Haver, KPMG

FIGURE 5
Selected Financial Market Indicators



Source: WSJ, FRB, Haver, KPMG

Financial conditions have become less accommodative in response to the conflict in Iran, but AI-related optimism continues to support strength in equity valuations.

Unsurprisingly, rising inflation expectations, tighter policy rates, and elevated risk premia have seen financial conditions tighten during the second quarter of 2026 compared to the start of the year.

Government bond yields have risen in most markets. Real long-term bond yields have also seen concurrent increases in markets such as the United States, United Kingdom and Japan, indicating that the rise in borrowing costs reflects not only higher inflation expectations but also an increase in underlying real rates – consistent with expectations of tighter financial conditions. China has been a notable exception, reflecting its low pre-conflict inflation and greater scope to cushion global energy supply shocks.

Similarly, corporate bond yields have also moved upwards, and spreads increased. Nonetheless, corporate borrowing has strengthened in the first part of the year, as investors remain confident in the positive impact of AI.

Meanwhile, equities markets have largely shaken off jitters from the Iran conflict. Despite falling initially, markets have generally recovered, also fuelled by the impact of AI, which have pushed up valuations to elevated levels.

By contrast, gold prices have fallen substantially, following unprecedented strength last year. Despite being considered a 'safe-haven' asset, the value of gold has fallen sharply as investors sell holdings to raise liquidity, and in response to higher interest rates. Furthermore, central bank gold purchasing patterns reversed in 2026. Following consistent net buying throughout 2025, World Gold Council data to April 2026 show a shift in behaviour, with net sales recorded in two of the first four months of 2026.

Box A: Geopolitical development and outlook

Contributed by Jon Berry, Geopolitics Lead, KPMG South ASPAC

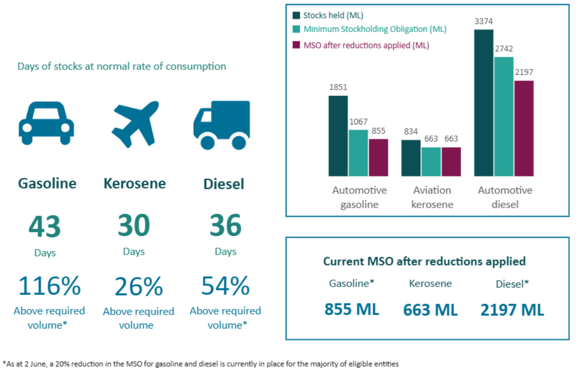
Cascading impacts from conflict in Iran

Conflict in the Middle East has had a range of implications for Australia in 2026, from energy security to the agricultural outlook to the growing importance of regional diplomatic links. The federal government has responded in a variety of ways, including via measures in the Budget. Depending how the ceasefire and further negotiations unfold over the coming weeks and months, these implications – and the policy actions taken in response – will impact Australian companies and the broader economy in a variety of ways.

Energy security

Since the beginning of the conflict, supply of oil, natural gas and refined fuels has been disrupted. Prices have risen, and governments around the world have moved to reduce demand and safeguard supply. These measures have included record drawdowns on global oil reserves, work from home orders and public transport subsidies, as well as governments both restricting energy exports and purchasing fuel cargoes on the open market. Although oil prices have come down since early June, these policy moves reveal a real anxiety over the cost and availability of energy, especially for countries that import most of the fuel that they need.

FIGURE A1
Fuel Stocks Held Under the Minimum Stockholding Obligation, 2 June



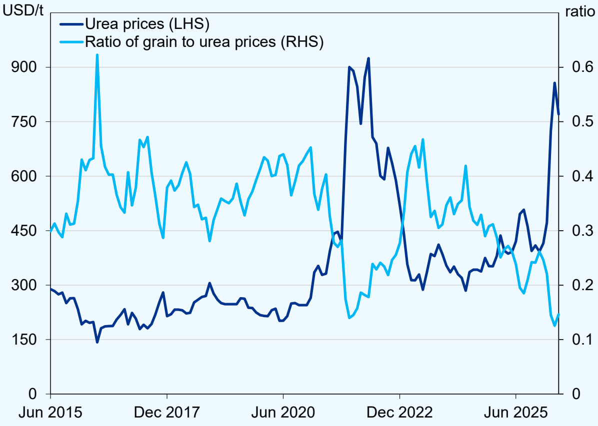
Source: DCCEEW

To address this anxiety, the federal government has strengthened efforts to report publicly on national fuel stocks. Other policy responses to support energy resilience have included a state-operated diesel fuel reserve, and funding to help private sector firms increase their fuel refining and storage capacity.

Agricultural outlook

Australia's agricultural sector has been particularly affected by the Iran conflict. Because of production and shipping disruptions, farm industries face price and supply challenges in multiple input categories, including fuel, fertiliser (see Figure A2) and equipment.

FIGURE A2
Urea and Ratio of Grain to Urea Prices



Source: World Bank, KPMG, Haver

In the last weeks of June, urea and energy costs retreated from their peaks, but the impacts of the period of high prices have yet to wash through agricultural systems.

The longer it takes for these disruptions to dissipate, the more difficult the situation will become.

However, the impact of the conflict on Australia's agricultural exports is a more complex issue. On one hand, global food prices are expected to continue to rise, as farm industries all over the world grapple with the cost pressures that have resulted from the war, as well as a strong anticipated El Niño weather event. This means that Australian exporters may be able to secure attractive prices for their goods. But on the other hand, an expected slowdown to economic growth in Australia's key Asian markets could translate into lower demand for premium Australian food and fibre exports.

Regional ties

As the Iran conflict unfolded, Australia and many other countries realised just how dependent they have become on fuel, fertiliser and other key commodities imported from other countries. Because of this dependence, the federal government has sought to bolster ties with key trading partners, including Singapore, Brunei, Malaysia and Indonesia. These international conversations have reportedly served to highlight the complementary trade relationships that Australia maintains with these countries. All countries concerned have made it a point to mention Australia's importance as a source of natural gas and food exports, while Singapore, Indonesia, Malaysia and Brunei provide refined fuels and fertilisers.

Implications for Australia

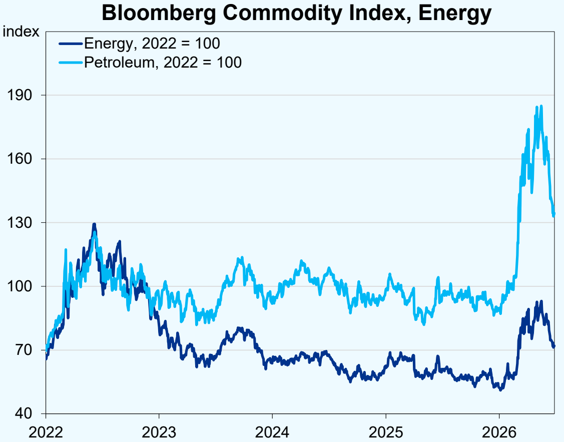
The conflict drives home how much Australia relies on global supply chains for critical inputs, even as it benefits from strong demand for some exports. Policy responses are addressing the need for resilience, but risks to growth and inflation remain. Businesses need to strike a balance between navigating near-term disruption while positioning for a more fragmented and uncertain future.

Box B: Commodity and transportation prices

Some commodities saw a sharp re-pricing in the wake of the Iran conflict, but the impact so far has been uneven.

Since the start of 2026, energy and petroleum prices showed the clearest war-driven spike, rising sharply from late February before easing back more recently. This pattern reflects an initial geopolitical supply shock consistent with past conflicts, but with prices now partially unwinding as markets adjust and supply concerns stabilise.

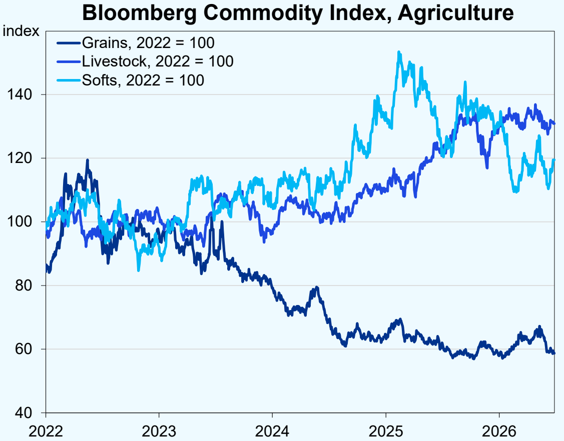
FIGURE B1
Bloomberg Commodity Index, Energy



Source: Bloomberg, KPMG

Meanwhile, industrial metals and agriculture have responded more gradually. However, the impact of high energy and fertiliser costs are likely to be passed on, even as the severity of the shock fades, through their impact on production decisions.

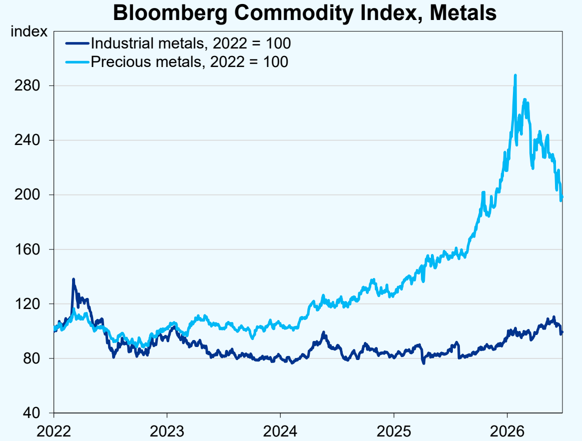
FIGURE B2
Bloomberg Commodity Index, Agriculture



Source: Bloomberg, KPMG

Taken together, higher oil and agricultural prices will flow through to higher global inflation. Developing nations will feel these pressures more acutely, with energy and food forming a larger proportion of the household consumption basket. Furthermore, economies in Asia will be more exposed to supply disruptions in the Middle East.

FIGURE B3
Bloomberg Commodity Index, Metals



Source: Bloomberg, KPMG

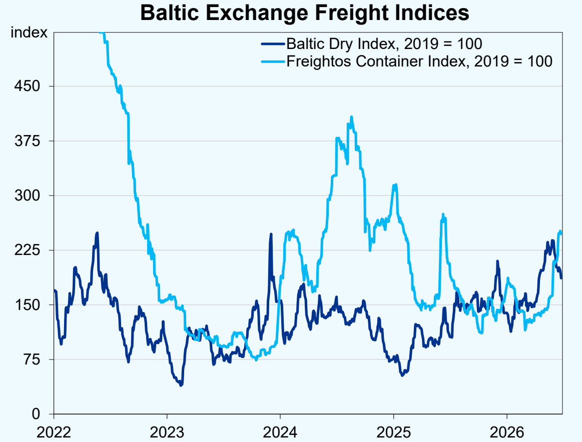
After an extraordinary surge in prices over the last two years, precious metals did not show a typical safe-haven rally following the outbreak of conflict. Instead, prices have trended sharply downward. This follows a moderation in central bank purchases of gold, which supported recent rises, as well as waning consumer demand. Recent price movements have been more influenced by monetary policy expectations, as opposed to the usual factors.

As with other recent supply shocks, transportation costs have also responded sharply.

At it's peak in early June, the Baltic Dry Index – which tracks shipping costs for raw materials – had risen by more than 50% compared to February. Despite cooling through the month, the index remained elevated at the end of June.

By contrast, the Freightos Container Index – which tracks container shipping rates for finished and semi-finished goods – has yet to reflect the easing of tensions and remained more than 70% higher than pre-war levels as of late June.

FIGURE B4
Baltic Exchange Freight Indices



Source: The Baltic Exchange, Haver, KPMG

ASPAC outlook

Growth across ASPAC in early 2026 was more mixed, with high-tech economies such as Taiwan, South Korea, Singapore and Japan recording solid growth, driven by AI-related exports and advanced manufacturing, while signs of moderation or weakness were seen across the rest of the region.

Despite prolonged geopolitical tensions and rising fuel costs weighing on the global economy, it is encouraging to see growth sustained across much of the region, although the global outlook for 2026 remains uneven. In particular, economies such as the Philippines could be more vulnerable to oil shocks, due to their heavy reliance on fuel imports from the Middle East.

- ***China***: GDP growth strengthened in the March quarter, accelerating to 5.0% over the year from 4.5% in the December quarter. Growth in services was the primary driver, with China's tertiary industry expanding 5.2%, outpacing both the secondary and primary industries. Price dynamics also improved, with producer prices rising 3.9% year-on-year in May, up from 2.8% previously, following a prolonged deflationary period. However, this acceleration was partly driven by higher energy prices linked to geopolitical tensions, rather than a rebalancing of supply and demand. Meanwhile, annual CPI held steady at 1.2% in May, while the People's Bank of China kept its benchmark policy rates unchanged at 3.0% in June for the 13th consecutive month.
- ***Japan***: In the March quarter, real GDP rose at an annualised rate of 1.8% (revised down by 2.1%), still exceeding market expectations of 1.7% and marking a second consecutive quarter of growth. This downgrade reflected weaker capital investment (revised from +0.3% to −0.7%), while private consumption remained unchanged at 0.3% quarter-on-quarter. Meanwhile, Japan's exports increased by 14.8% year-on-year, driven by strong demand for machinery and transport equipment. Meanwhile, imports grew more modestly, rising only by 9.7% over the same period.
- ***South Korea***: GDP grew by 1.8% (revised up by 0.1%) in the March quarter, the strongest pace in 5.5 years, lifting annual growth to 3.8%. The expansion was driven by strong semiconductor exports and a recovery in domestic demand. Meanwhile, the headline CPI rose 3.1% year-on-year (the fastest since March 2024), driven by higher oil prices reflecting the impact of the US-Iran conflict on global energy markets.
- ***Taiwan***: Marking the fastest pace of expansion in nearly four decades, Taiwan's revised GDP grew 14.6% year-on-year in the March quarter, surpassing market expectations. This was supported by strong AI-driven export growth, solid domestic demand, and a rebound in investment. Likewise, Taiwan's exports surged 51.7% year-on-year in May, driven by strong AI-led demand.
- ***Singapore***: The economy grew by 6.0% year-on-year in the March quarter, exceeding expectations. This growth was driven by strong AI-related demand, boosting wholesale trade alongside manufacturing. Consequently, the Ministry of Trade and Industry maintained its 2-4% growth forecast, while also noting rising downside risks. Meanwhile, both core and headline inflation held steady at 1.4% and 1.8% year-on-year, respectively, in May, both coming in below expectations of a modest acceleration.
- ***Hong Kong****:* Real GDP grew strongly 5.9% over the year to the March quarter, the fastest pace in nearly five years. Meanwhile, seasonally adjusted GDP rose 2.9% on a quarterly basis, driven by strong external trade and improving domestic demand.
- ***New Zealand****:* New Zealand's GDP rose by 0.8% quarter-on-quarter in the March quarter (within 0.4% to 1.0% forecasts), lifting annual growth to 1.5%. Growth was broad-based, with manufacturing sector reporting the largest positive contribution (+1.9%), showing the economy is regaining momentum as lower interest rates flow through.
- ***Indonesia***: GDP grew 5.6% yearly in the March quarter, supported by accommodation and food services, and government spending. However, GDP fell by 0.8% quarterly, with declines in production in mining and quarrying. Meanwhile, annual CPI rose to 3.1% in May, while Bank Indonesia continued to increase its policy rate by 25 bps to 5.75% in June.
- ***Vietnam***: The economic growth slowed in the March quarter, with full year growth increasing 7.8% compared to 8.5% in the December quarter. This moderation was broad-based across major sectors, pointing to a mild cooling in growth momentum.
- ***Philippines***: GDP growth for the March quarter 2026 fell short of expectations, rising only 2.8% year-on-year, with weakness broad-based across most expenditure categories. Through the quarter, the economy expanded by 0.9%. Furthermore, annual inflation unexpectedly eased to 6.8% in May from 7.2% in April, driven by slower rises in food and transport costs.
- ***Malaysia***: Driven by strong domestic demand and exports, Malaysia's GDP grew 5.3% year-on-year in the March quarter. However, rising energy costs and ongoing supply chain disruptions are now posing increasing challenges to fiscal management and industrial stability.
- ***Thailand***: Thailand's GDP grew by 2.8% in the first quarter of 2026, accelerating from 2.5% in the previous quarter. This increase was supported by robust investment growth, which reached 9.9%, up from 8.1% in the previous quarter, marking Thailand's highest growth rate in a decade.

02

Australia overview

Economic activity

Growth in the Australian economy slowed by more than expected in the March quarter, with pre-existing domestic fragilities looking to be compounded by the conflict in Iran.

Over the March quarter 2026, real GDP expanded by a modest 0.3% in seasonally adjusted terms. This was below market expectations, which had already anticipated a slowdown in growth to 0.5%. Consequently, the pace of growth was significantly less than the 0.9% seen in the December quarter (revised up from 0.8%).

On an annual basis, the economy expanded by 2.5%, which was also lower than the consensus forecast of 2.7%, albeit still in line with the 2.5% pace of annual growth seen last quarter. While the economy expanded only modestly, it was still sufficient to keep inflation elevated.

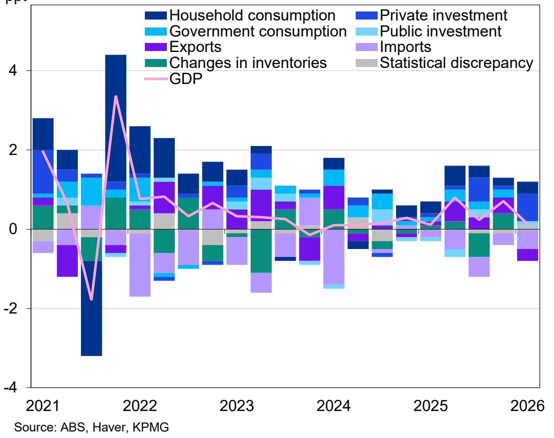
Looking at the contributors to quarterly GDP growth, we find that:

- Private investment added significantly to growth (+0.7ppt), although this was driven by import-intensive data centre investment, so the increase in imports offset much of its effective contribution to GDP.
- Household consumption added 0.3ppt to growth. We note however it would have been much weaker if not for technical factors, with measured electricity spending rising due to the cessation of government rebates. Additionally, demand this quarter was supported by the stockpiling of food (in cyclone affected regions) and fuel (reflecting supply concerns due to the conflict in Iran).
- Public demand made zero contribution to growth. There was a modest fall in government consumption, reflecting the end of electricity subsidies, while public investment rose. A key driver of this increased investment was spending on imports of defence weapons platforms, rather than domestic activity.

FIGURE 6

Contribution to Quarterly GDP Growth

Seasonally adjusted, chain volume measures



Source: ABS, Haver, KPMG

- Net trade subtracted 0.8ppt from GDP growth, as exports fell by 1.1%, with imports also rising by 2.1%. Consequently, Australia recorded its first trade deficit since the December quarter 2017. Weather-related disruptions were responsible for a reduction in iron ore and coal exports, which would have supported a build-up of inventories instead.
- Overall, changes in inventories made no contribution to growth this quarter. Although mining inventories increased, non-mining inventories were run down. Both public authorities and manufacturing inventories decreased due to demand for non-monetary gold.

These latest figures do not suggest that an improvement in growth is likely over the near term. Other aspects of the data also reflect this challenging picture:

- GDP per capita fell by 0.1% over the quarter, following a 0.5% rise in the December quarter. Through the year, GDP per capita has risen by 1.0%. This was the ninth quarter in the past 13 quarters where GDP per capita has declined.
- Labour productivity declined, with GDP per hour worked falling by 0.6% over the quarter, after being flat in the December quarter. This translates into a 0.3% rise through the year.
- The government share of spending remains close to record highs, at 28.5% of GDP. While this has stabilised, it remains a level which continues to crowd out the private side of the economy.

Turning to the household sector, the latest National Accounts data also reinforced the pressures that many Australians are facing:

- Household spending rose by 0.5%, following a 0.4% rise last quarter. However, this was driven by a 0.8% increase in essential spending, with only a marginal 0.1% rise in discretionary spending. This was consistent with weakened consumer confidence, reflecting the initial impact of the February cash rate increase and the onset of the Iran conflict.
- Meanwhile, the household saving ratio fell to 6.2%, from 7.0% last quarter, although this was little changed from the 6.1% seen six months prior. This comes as the 1.1% rise in nominal household consumption outpaced the 0.4% rise in gross disposable income.
- Interest paid on dwellings rose 5.1% in the March quarter, although it was still down 2.3% through the year. This incorporated the impact of the increase to the cash rate in February, with subsequent cash rate increases in mid-March and early May looking to push interest payments higher in coming quarters.

Over the quarter, compensation of employees (COE) rose 1.2%, following a 1.5% rise in the December quarter. Through the year, the pace of growth in COE eased for the second consecutive period to 6.0%.

Looking in more detail, through the quarter:

- Private sector COE rose 1.5%. This was driven by strength in the *Professional, scientific and technical services*; *Construction*; and *Administrative and support services* sectors.
- Meanwhile, public sector COE was flat, with rises in Victoria and South Australia offset by weakness in Queensland and New South Wales.
- All states and territories saw a quarterly rise in COE, led by Victoria (+1.7%), followed by South Australia (+1.6%) and Western Australia (+1.5%).

KPMG considers this rate of growth is unsustainable at current levels of employment, without higher levels of productivity (or Australia benefiting from an improvement in our terms of trade, which we believe is unlikely in the near term).

Meanwhile, business profitability as measured by gross operating surplus (GOS) was flat during the quarter.

- Private non-financial corporations GOS decreased 1.1%. The fall for *Mining* was due to decreased prices and sales volumes for iron ore and coal. On the other hand, non-mining GOS rose, driven by *Construction*; *Information media and telecommunications*; *Wholesale trade*; and *Manufacturing*.
- Other sectors' GOS rose by 1.5%, with rises for financial corporations and dwellings owned by persons, partially offset by a fall for public non-financial corporations.

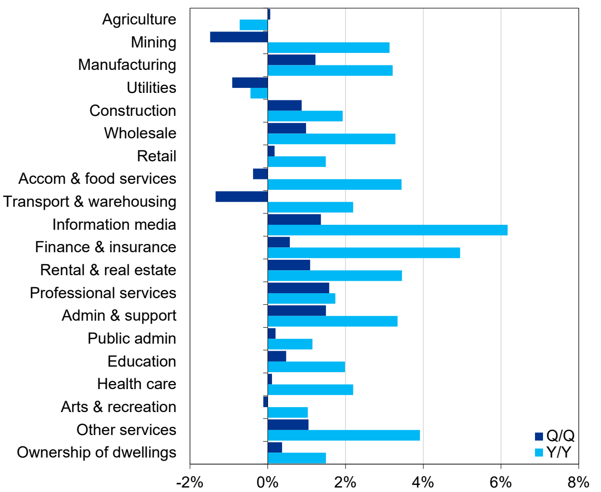
Consequently, GOS was up 4.2% through the year, with the pace of annual growth slowing, after accelerating for the prior three quarters.

Production

Over the March quarter, gross value added (GVA) rose by 0.3%, with 14 out of the 19 industries recording an increase in GVA. Growth was supported by:

- *Professional, scientific and technical services* (+1.6%), due to demand for engineering design and IT consultancy.
- *Information media and telecommunications* (+1.4%), due to increased data centre activity.
- *Construction* (+0.9%), with higher activity in residential constriction, as well as data centre projects.
- *Manufacturing* (+1.2%), which saw increased demand for fertiliser production and petroleum refining.

FIGURE 7
Industry Gross Value Added, Mar 2026



Source: ABS, Haver, KPMG

By contrast, household-facing sectors saw weakness in the quarter, consistent with softening discretionary spending:

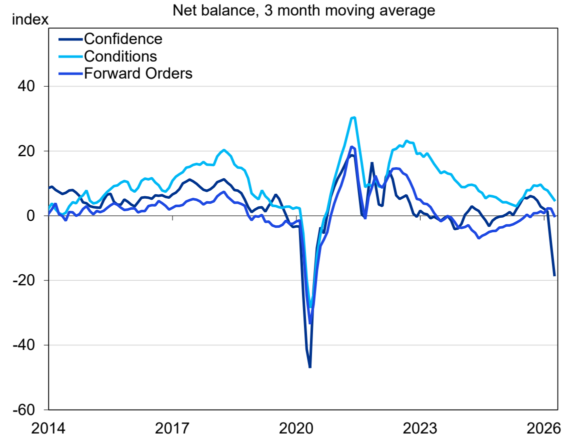
- *Retail trade* (+0.2%) saw only modest growth, with increases in food retailing partly offset by a fall in demand for new passenger vehicles.
- *Accommodation and food services* (-0.4%) experienced lower demand for cafes and restaurants.
- *Arts and recreation services* (-0.1%) fell, driven by gambling activities.

The most significant fall, however, was seen in the *Mining* sector (-1.5%). This was predominantly due to adverse weather events which impacted production of various commodities, particularly coal.

Meanwhile, producer price inflation (as measured by final demand) eased to 3.0% in the year to the March quarter. This was the slowest annual rise since the September quarter 2021, supported by a significant appreciation in the Australian dollar since mid-2025.

This was also the weakest pace of quarterly growth in producer prices (+0.4%) in five years. Price rises during the March quarter were mainly driven by the construction and services industries, tied to demand for residential property.

FIGURE 8
Business Sentiment
Net balance, 3 month moving average



Source: NAB, Haver, KPMG

Looking ahead, business confidence (as measured on a three-month moving average basis) has deteriorated significantly, slipping to -18.3pts in April, and is now deep within pessimistic territory. This reading was also the worst since the beginning of the COVID-19 pandemic, reflecting the disruption and ongoing uncertainty stemming from the Iran conflict.

Turning to commodities, the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES) now anticipates the gross value of agricultural production will fall 5% to $98 billion in FY2026–27, after reaching a peak of $104 billion in FY2025–26. This comes as falling production is expected to outweigh higher prices for crops, with ABARES noting that production estimates could fall further if an El Nino event emerges.

The value of agriculture exports is also expected to fall to $74.8 billion, due to lower livestock and crop exports. Meanwhile, average broadacre farm business profit is forecast to fall by 70%, due to a combination of lower revenue and higher input prices.

Meanwhile, prior to the outbreak of the Iran conflict, the Department of Industry, Science and Resources had been anticipating that the nominal value of resource and energy exports would fall 2.3% to $374 billion in FY2026–27, from an anticipated $383 billion in FY2025–26. This reflects an upward revision, due to higher gold prices and resilience in the price of iron ore.

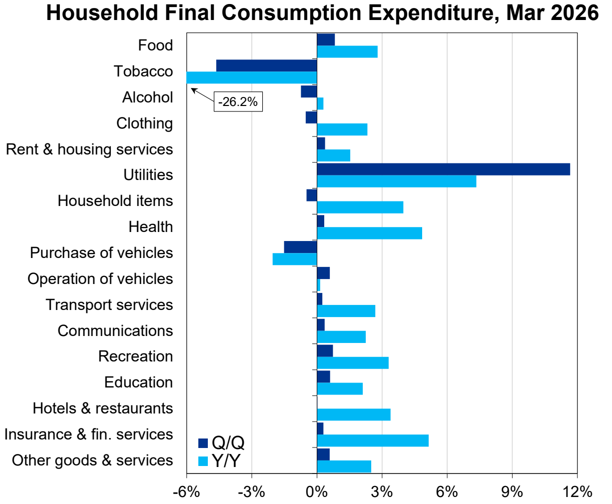
Household consumption

Household consumption, as measured by household final consumption expenditure (HFCE), rose by 0.5%, following a 0.4% rise in the previous quarter. This movement was mainly due to a 0.8% rise in essential spending, with discretionary spending rising by a marginal 0.1%. On an annual basis, HFCE rose by 2.5%, unchanged from the prior December quarter.

The quarterly rise in essential spending was due to:

- *Electricity, gas and other fuels* (+11.7%), due to higher 'out-of-pocket' spending by households on electricity. This can be attributed to the cessation of government subsidies, which previously meant some 'spending' on household electricity was included as government consumption instead.
- *Food* (+0.8%) and *Operation of vehicles* (+0.6%) both saw stockpiling by households during the quarter. The increased purchase of food reflected precautionary behaviour ahead of forecast cyclones, while the increased demand for fuel was due to concerns over potential supply shortages.

FIGURE 9
Household Final Consumption Expenditure, Mar 2026

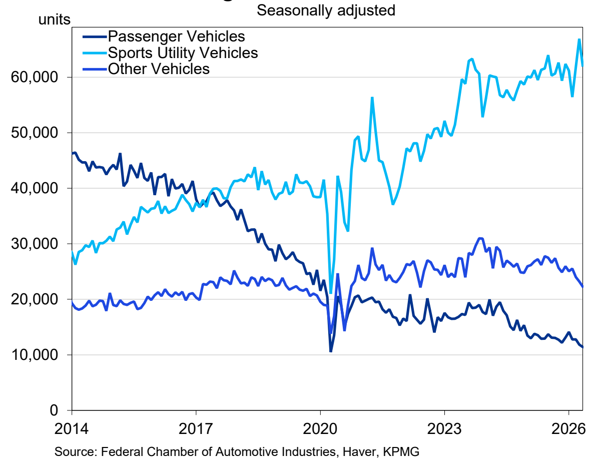


Source: ABS, Haver, KPMG

Overall growth in HFCE was partially offset by:

- *Purchase of vehicles* (-1.5%), reflecting weak car sales in the quarter.
- *Cigarettes and tobacco* (-4.6%), noting the dominance of illicit sources remains a challenge for accurate measurement. March data also included new estimates by the ABS on illicit tobacco, which found that the quantity of nicotine consumed in 2025 was almost 40% higher than 2017. During that time, illicit sources as a share of total tobacco consumption increased from 12% to 80%. This is consistent with a growing price differential, with legal tobacco products nearly three times more expensive in 2025 compared to 2017, but illicit products seeing little change.

FIGURE 10
Passenger Vehicles and SUV Sales
Seasonally adjusted

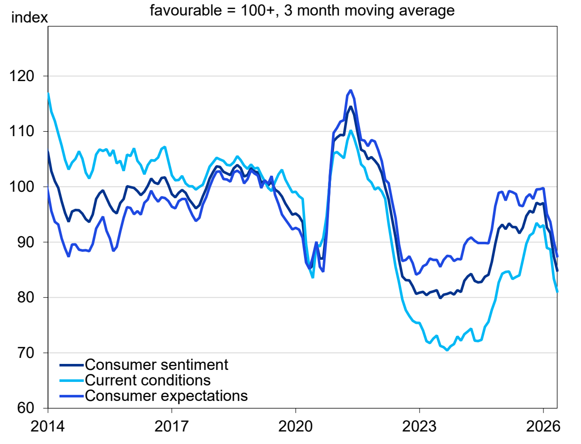


Source: Federal Chamber of Automotive Industries, Haver, KPMG

Looking ahead to more timely data:

- Data from the Monthly Household Spending Indicator recorded a 1.3% rise in nominal spending in May, though this follows a 1.1% fall in April, which coincided with the temporary reduction in the fuel excise.
- The number of new vehicles sold has been trending downwards, with 95,100 sales (measured in seasonally adjusted terms) during May.
- Consumer sentiment, as measured by the Westpac–Melbourne Institute monthly survey, has continued to decline steeply. On a three-month moving average basis, it fell to 84.9pts in May, deteriorating for the fourth consecutive month. It is now at its lowest level since September 2024. This decline in confidence reflects the impact of elevated inflation, three consecutive interest rate hikes, a sharp rise in fuel prices, as well as ongoing uncertainty stemming from the conflict in Iran.

FIGURE 11
Consumer Sentiment
favourable = 100+, 3 month moving average



Source: Westpac - Melbourne Institute, Haver, KPMG

Investment

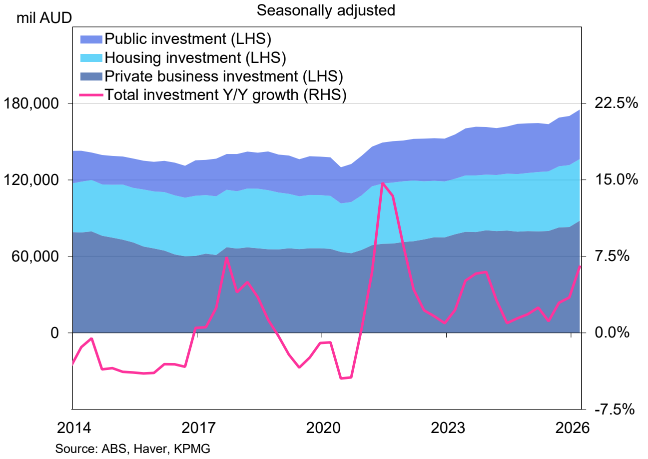
Investment activity, as measured by gross fixed capital formation (GFCF), rose by 3.0% in the March quarter. This saw annual growth accelerate to 6.5%, from 3.5% in the previous quarter, and its fastest pace since the December quarter 2021.

Private investment increased 3.6% in the March quarter, the largest quarterly increase in five years. Consequently, annual growth in private investment accelerated to 8.1%, from 4.9% last quarter.

Overall, the quarterly movement was driven by:

- *Machinery and equipment* (+16.3%) saw a sharp rise, reflecting elevated investment in data centres in New South Wales and Victoria.
- *Dwellings* (+0.7%), driven by increased activity on alterations and additions, as well as large apartment projects. This was partly offset by a fall in new and used dwellings.
- Meanwhile, *Ownership transfer costs* (-4.1%) saw a notable fall.

FIGURE 12
Real Public and Private Investment
Seasonally adjusted



Source: ABS, Haver, KPMG

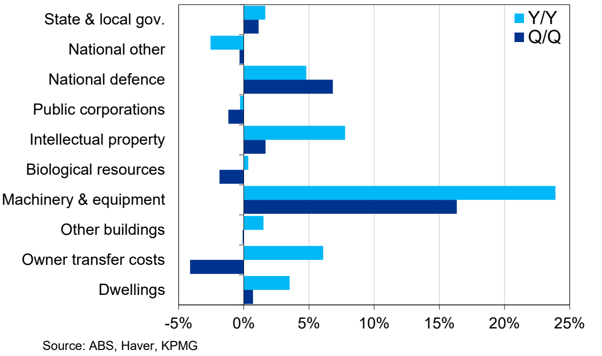
Public investment grew by 0.9%, unchanged from the pace seen last quarter. Through the year, it was up 1.1%, which was the first positive annual growth rate in a year.

The rise this quarter was due to:

- *National defence* (+6.8%), due to imports of defence weapons platforms.
- *State and local general government* (+1.1%), reflecting continued work on transport and health projects.

Overall, in the March quarter, private investment added 0.7ppt to GDP growth, though a large proportion of this was offset by a reduction in net trade, as most data centre equipment is imported. Public investment added a modest 0.1ppt to growth; however, similar to private investment, part of this was offset by imports of defence equipment.

FIGURE 13
Investment Growth, Mar 2026



Source: ABS, Haver, KPMG

Returning to the private sector, investment by businesses, as measured by real private new capital expenditure (capex), rose 6.5% in the March quarter. It is now up 14.6% through the year.

This quarterly rise was driven by:

- *Equipment, plant and machinery* (+18.1%), mainly driven by non-mining equipment and machinery, which was up 20.1% during the quarter. This reflected higher investment in data centres, particularly the fit-out of server racks and other processing equipment. Through the year, real capex on *Equipment, plant and machinery* was up 31.0%.
- *Buildings and structures* (-3.8%) partly offset this growth, as large projects reached completion in both non-mining (-4.3%%) and mining (-2.9%) sectors.

Looking across the industries, the strongest growth was seen in *Information media and telecommunications*, consistent with the elevated spending on data centres. This saw capex nearly double in the March quarter (+96.1%), to be up 190.1% compared to a year ago.

Most of this investment was in New South Wales (+22.1%) and Victoria (+12.7%), which recorded the largest rises in capex. South Australia (+0.2%) was the only other state or territory to see a rise in capex over the quarter.

Moving forward, this March data also showed that businesses have revised up their expected nominal capex spend for FY2025–26 to $207.6 billion, 4.5% higher compared to the last survey. Additionally, they now expect nominal capex of $173.4 billion in FY2026–27. This is 9.9% higher than the estimate reported from the previous survey.

This increase in expectations also reflected ongoing strength in the data centre sector.

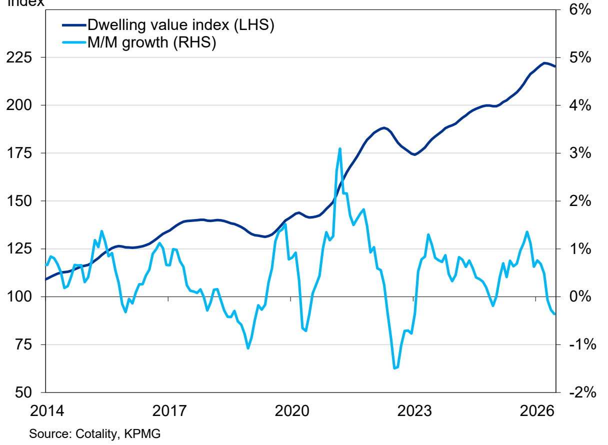
Looking at the residential property sector, there has been a clear reversal of momentum, with national home prices falling 0.4% in the month of June. This was largest monthly fall since December 2022, according to Cotality data.

Sentiment in the housing market has been dampened, following the 75bps of interest rate rises delivered across three cash rate hikes in February, March, and May. Changes to capital gains tax and negative gearing introduced in the FY2026–27 Federal Budget have also started to temper investor demand. Consequently, national prices have fallen 0.7% over the three months to June, with a 1.1% quarterly rise in regional values more than offset by the 1.3% fall seen across the combined capitals.

This downturn was led by the major capital cities, with Sydney (-3.2%) and Melbourne (-2.6%) seeing notable price falls over the three months to June. Canberra (-1.3%) was the only other capital city to see a price fall during this period.

Conversely, growth in the mid-sized capitals proved to be more resilient, although momentum is also fading. The fastest pace of growth over the last three months was seen in Darwin (+5.0%), followed by Perth (+2.0%). Price rises were also seen in Hobart (+1.4%), Adelaide (+1.3%) and Brisbane (+1.3%).

FIGURE 14
Home Value Index



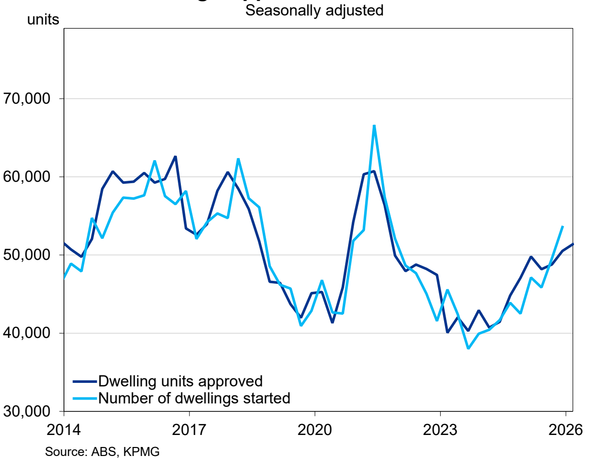
Source: Cotality, KPMG

On an annual basis, all capital cities except Melbourne still saw price growth, supported by the stronger performance of the market during the second half of 2025. Overall, national price growth slowed to 7.3% in May, after peaking at 10.3% in February.

Perth saw the strongest growth through the year, with prices up by a remarkable 23.9%. Both Darwin (+19.8%) and Brisbane (+17.4%) also saw extremely strong annual growth. This was followed by Adelaide (+11.6%), Hobart (+9.3%), and Canberra (+2.9%).

By contrast, the largest capitals saw the weakest annual performances, with Sydney (+0.3%) seeing a marginal rise and Melbourne (-0.9%) recording a modest fall.

FIGURE 15
Dwellings Approved and Commenced
Seasonally adjusted



Source: ABS, KPMG

Although the data is lagged, it does show an improvement in housing supply. The number of new dwelling units approved increased by 1.7% to 51,380 in the March quarter, the highest level since the September quarter 2021. This was 3.2% higher than the corresponding period of 2025.

Looking at the composition of approvals:

- *Houses* was up 4.9% in the March quarter, reaching 30,610 approvals.
- *Other dwellings* was down 2.7% during the quarter, with 20,770 approvals.

Consistent with the upward trend in approvals, building activity has also been expanding. The number of dwelling units commenced rose 8.0% in the December quarter 2025 to 53,570 units. This was the highest level since the September quarter 2021 and is 26.1% higher than a year ago.

The rise in residential building activity was due to:

- *New private sector other residential* commencements, which rose 23.4% to 23,850 dwellings in the December quarter.
- *New private sector houses* partially offset this rise, falling 0.9% to 28,470 units.

Housing affordability remains a key issue and is highly dependent on a timely expansion in supply. Looking ahead, building activity is expected to face increasing downward pressures from higher interest rates, softer housing market returns, and the impact of the Iran conflict on input costs.

This poses a further challenge to meeting the Commonwealth government's housing supply target of 1.2 million new homes over the five years to June 2029. The latest forecast by the National Housing Supply and Affordability Council, released at the end of April, suggests this target would only be met in September 2030, more than a year beyond the target date.

Net exports

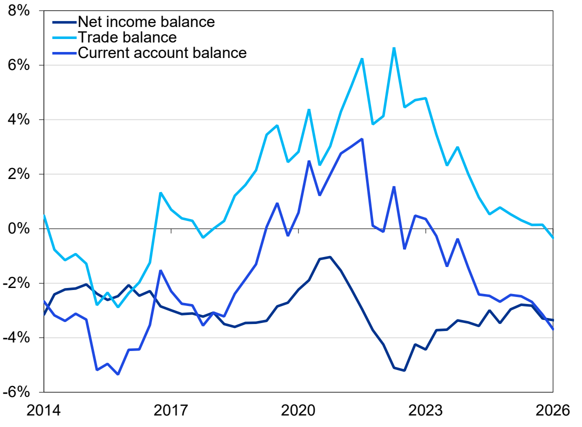
Net trade subtracted 0.8ppt from quarterly GDP growth, due to a 1.1% fall in exports and a 2.1% rise in imports. This fall in exports marked the largest quarterly decline in two years, led by falls in coal (-6.8%) and mineral ores (-1.3%). The rise in imports was mainly due to the rise in imports of capital goods (+6.3%).

In detail, exports of goods fell 0.8% due to a decline in non-rural exports, particularly coal and iron ore. This decline was driven by tropical cyclones Koji in Queensland and Mitchell in Western Australia, which disrupted operations at major coal and iron ore export ports in those regions. Rural goods also contributed to the fall, while non-monetary gold exports rose with demand, especially from Asia.

Exports of services also fell 2.1%, with weakness observed in education and other personal travel due to lower student numbers and weaker overseas arrivals.

At the same time, imports of goods rose 1.4%, led by a rise in capital goods, with record imports of computing equipment. Meanwhile, intermediate goods imports were stable, as many scheduled shipments of fuel and fertiliser were already in transit prior to the closure of the Strait of Hormuz. However, imports of consumption goods fell, driven by lower demand for motor vehicles.

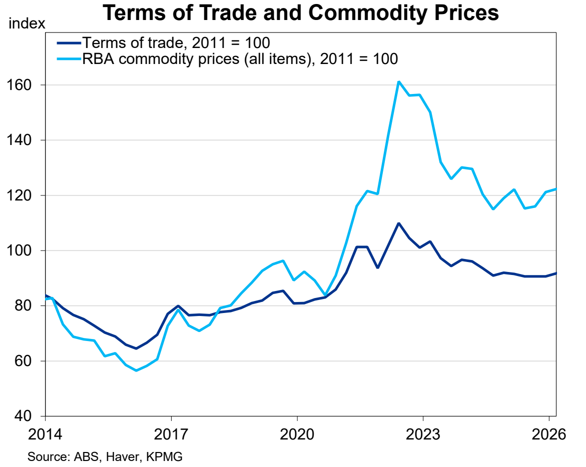
FIGURE 16
Current Account Balance
Percent of nominal GDP



Source: ABS, Haver, KPMG

Imports of services rose 3.8% across all categories, as the appreciation of the AUD supported higher import volumes for transport, travel and other professional services.

FIGURE 17
Terms of Trade and Commodity Prices



Source: ABS, Haver, KPMG

Australia's current account balance fell for the fourth consecutive quarter, further widening its deficit. This was mainly due to the balance on goods and services shifting into deficit for the first time since the December quarter 2017, alongside a slight widening in the net primary income deficit.

On a seasonally adjusted basis, the current account deficit increased by $4.1 billion, from the revised December quarter deficit of $23.0 billion to $27.1 billion in the March quarter 2026. As a share of nominal GDP, the current account balance declined to -3.7%, marking the largest deterioration observed since the December quarter 2017.

EXTERNAL DEMAND ASSUMPTIONS	Q2-2026 (a)	Q3-2026 (f)	Q4-2026 (f)	Q1-2027 (f)	Q2-2027 (f)
Exchange rate (AUD/USD)	0.71	0.71	0.71	0.71	0.71
Coal prices (USD/tonne)					
Thermal coal price – Newcastle	140	126	127	128	127
Semi-soft coking coal price	238	241	242	245	246
Gold price (USD/oz)	4,482	4,081	4,124	4,177	4,221
Dalian Iron Ore 62% Futures	104	99	98	98	97
Oil prices (USD/barrel)	91	70	69	68	67

Note: Average over period.

The terms of trade rose by 1.1% in the March quarter. Despite a fall in export prices, import prices declined by more.

Export prices fell 0.1%, as there was a decline in iron ore prices due to oversupply concerns. Partly offset the fall in iron ore prices was rising lithium and coal prices. The increase in lithium prices was driven by stronger demand linked to battery production and electric vehicle manufacturing.

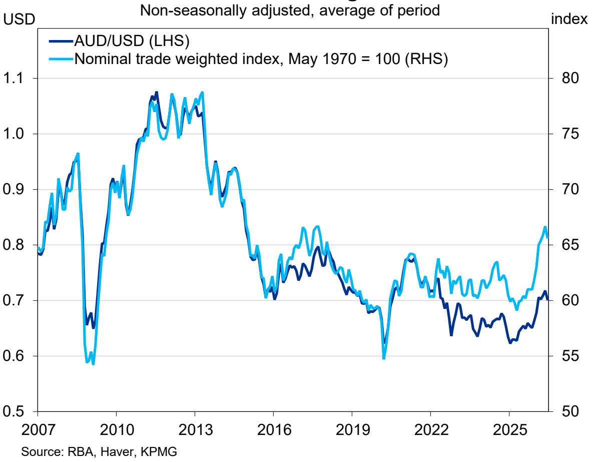
Import prices declined 1.2%, reflecting the strong appreciation of the Australian dollar, which led to significantly cheaper prices across all import service categories and most consumption and capital goods categories. Meanwhile, higher prices for intermediate goods such as fuels and fertilisers partly offset the fall due to the supply disruption caused by the Iran conflict.

The Australian dollar has appreciated since the beginning of 2026, rising from around US$0.68 in January to a peak of around US$0.72 in May, before easing to around US$0.70 in late June. Over the same period, the trade-weighted index (TWI) increased from 63pts in January to 67pts in May and moderated to around 66pts in June. This appreciation has been primarily driven by relatively higher domestic interest rates, which have supported capital inflows into Australian assets. Strong commodity demand has also provided some support, helping to keep the currency elevated despite global uncertainty.

FIGURE 18

Australian Exchange Rate

Non-seasonally adjusted, average of period



Source: RBA, Haver, KPMG

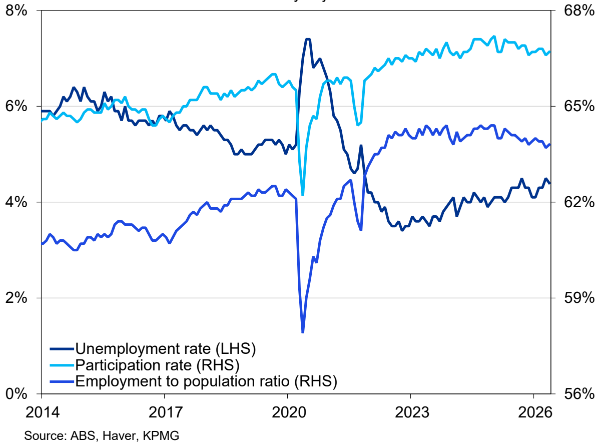
Labour market

Conditions in the Australian labour market have begun to soften in the June Quarter 2026, with employment conditions weakening notably in April before showing a modest recovery in May.

The latest data show that the unemployment rate edged down to 4.4% in May 2026, from 4.5% in April, but remains 0.3ppt higher than a year earlier. The increase to 4.5% in April marked the highest rate in the current cycle, and the highest level since November 2021.

The participation rate rose slightly to 66.7% in May 2026 from 66.6% in the previous month but was 0.3ppt lower than a year earlier. It nevertheless remains elevated relative to pre-pandemic levels. The employment-to-population ratio also edged higher to 63.8% in May from 63.7% in April but remained 0.5ppt lower than the same time last year.

FIGURE 19
Unemployment and Participation Rates
Seasonally adjusted



Source: ABS, Haver, KPMG

Despite the weaknesses observed in employment conditions in April, conditions improved modestly in May. Employment increased by around 40,300 people (0.3%) in May, driven primarily by a rise of around 35,200 in part-time employment, while full-time employment increased more modestly by around 5,200. As a result, annual employment growth rose to 1.0% in May compared with a year earlier, indicating a modest recovery. However, employment growth remains below the pace recorded in early 2026.

In contrast to the rise in employment, monthly hours worked declined by 1.1% in May, following the 0.9% increase recorded in April. The April rise was partly driven by fewer people taking leave during the Easter holiday period and instead working their usual hours, which temporarily boosted hours worked. The decline in May brings hours worked back in line with employment growth observed since mid-2022.

A similar easing is evident in broader measures of labour market slack. The underemployment rate edged up to 5.9% in May, pointing to a modest increase in spare capacity in the labour market, though it remains broadly unchanged from a year earlier.

Filled jobs rose 0.6% in the March quarter to reach 16.2 million and were 1.9% higher over the year. The number of public sector jobs increased by 0.1%, while the number of private sector jobs increased by 0.7%.

Looking ahead, the SEEK Employment Report for April 2026 showed that job advertisement volumes decreased 0.3% through the quarter, and down by 1.9% over the year.

Across industries, most sectors recorded growth in job advertisement volumes in April. *Construction and Industrial* sectors continue to drive much of the overall national growth, while the *Consumer Services* sector has also picked up, rising 1.4% over the quarter.

At the state and territory level, the monthly job advertisements increased across most regions, with the exception of the ACT, which declined by 0.7%. The strongest monthly gains were recorded in South Australia at 2.3% and the Northern Territory at 2.0%, supported by growth in construction-related industries

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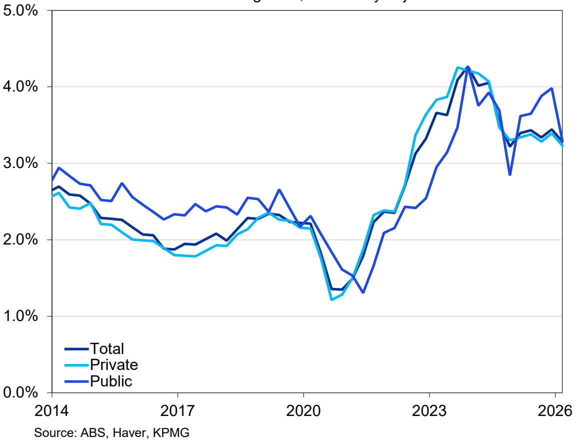
FIGURE 20
Wage Price Index by Sector
Year-ended growth, seasonally adjusted



Source: ABS, Haver, KPMG

Quarterly wages growth has been steady for a third consecutive quarter, rising 0.8% in the March quarter 2026. Annual wage growth slowed slightly to 3.3%, down from 3.4% in the December quarter 2025.

In quarterly terms, wages in the private sector increased by 0.8%, while public sector wages rose only 0.5% over the March quarter 2026.

Annual growth in private sector wages slowed to 3.2%, down from 3.4% in the December quarter, and public sector wage growth also slowed to 3.3% over the year to March 2026, down from 4.0% in the December quarter. However, this marked a fifth consecutive quarter in which public sector wage growth outpaced that of the private sector, although the gap has narrowed considerably.

In the March quarter 2026, almost two-thirds of jobs, or 61%, recorded annualised wage growth of more than 2% but less than 4%. A further 22% of jobs recorded annualised wage growth above 4%, marking the lowest share for this category since the June quarter 2022.

When considering industry wage growth*, Electricity, gas, water and waste* services recorded the strongest wage outcomes, with the highest quarterly and annual increases of 1.1% and 4.3%, respectively.

In terms of contributions to overall wage growth, which reflect both the relative size of an industry and the magnitude of wage changes, the *Health care and social assistance* industry remained the largest contributor, accounting for 19% of total growth and rising by 0.7% over the quarter. According to the ABS, this reflected a major Commonwealth-funded initiative in the early childhood education workforce, which supported wage increases in the private sector, while public sector growth was driven by wage gains among Queensland healthcare workers. The *Education and training* industry was the second-largest contributor, accounting for 11% of quarterly wage growth.

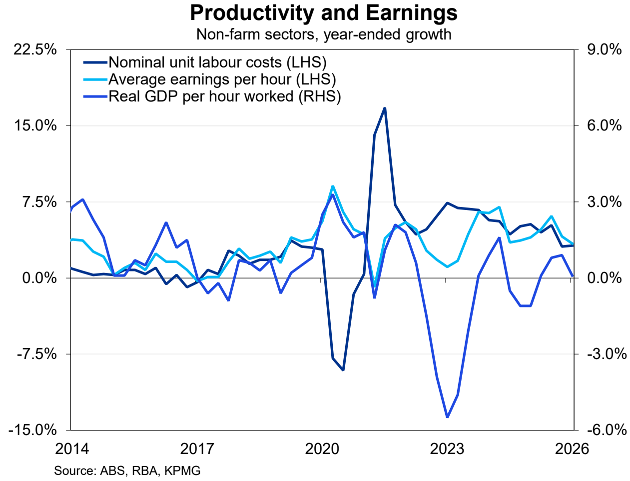
By state and territory, the Australian Capital Territory recorded the strongest outcomes in both quarterly and annual wage growth, at 0.8% and 3.7%, respectively. In contrast, New South Wales, South Australia and Western Australia recorded the weakest quarterly growth at 0.4%, and the Northern Territory the recorded lowest annual growth at 2.3%.

The Fair Work Commission announced a 4.75% increase to modern award wages from 1 July 2026. It also announced a 6% rise in the National Minimum Wage, lifting it to $1,004.90 per week, or $26.44 per hour, marking the first time it has crossed the $1,000 per week threshold. Even though the increase supports low-paid workers, the decision appears generous and will likely add to cost pressures for businesses, which may weigh on employment growth, particularly given weak productivity.

Alongside the WPI, which reflects a fixed composition of labour costs, it is also useful to consider nominal unit labour costs (NULC), which measure the cost of labour adjusted for productivity. As a result, there will be no change in NULC if there is an increase in average labour costs and a corresponding increase in labour productivity. In the March quarter, NULC increased by 3.2% over the year.

Real unit labour costs (RULC), the indicator of the average cost of labour per unit of output produced in the economy adjusted for price changes, re-confirmed a renewed increase in cost pressures on firms. RULC increased by 0.5% q/q in the March quarter 2026, following a decline of 0.7% in the December quarter. In annual terms, RULC rose by 0.5%.

FIGURE 21



Source: ABS, RBA, KPMG

Government

In the March quarter 2026, public sector demand did not contribute to GDP growth, as the rise in public investment of 0.9% was offset by a 0.2% decline in government consumption, leaving the overall contribution neutral.

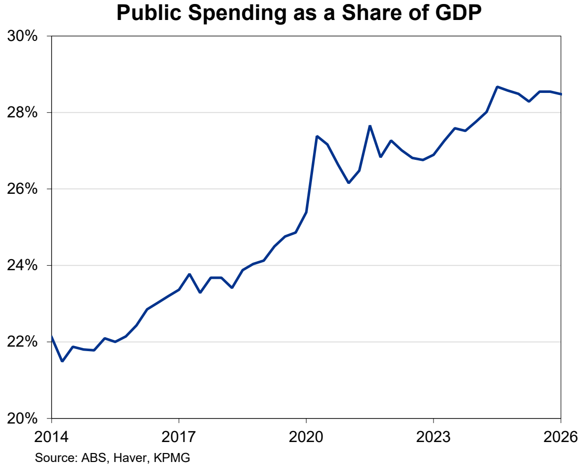
The fall in government consumption was driven by:

- Reduced social benefits to households from *State and local general government* following the end of energy bill relief.
- A decline in *National defence* spending in the quarter, although levels remained elevated over the year, increasing by 7.2%.
- This fall in *defence* was partly offset by higher *National non-defence* expenditure, reflecting increased non-employee expenses across several large government agencies, alongside a rise in social benefits to households linked to home and aged care.

In contrast, the rise in investment was supported by:

- Strength in *Defence investment*, which increased by 6.8% due to higher imports of weapons platforms.
- Higher *State and local general government investment*, which rose by 1.1%, driven by continued spending on transport and health infrastructure projects.

FIGURE 22
Public Spending as a Share of GDP



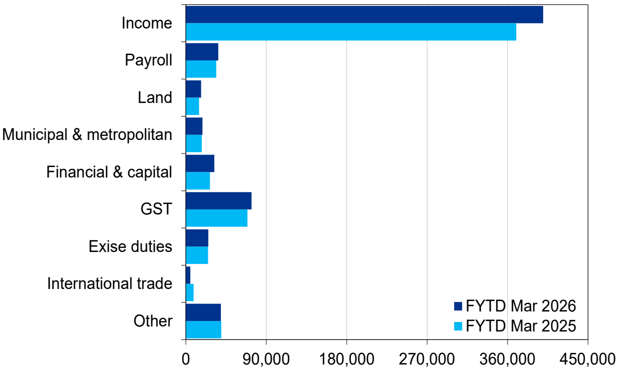
Source: ABS, Haver, KPMG

All non-market sectors contributed to GDP growth in the March quarter 2026. In real gross value-added terms, *Public administration and safety* expanded by 0.2% and *Education and training* rose by 0.5%, both unchanged from the previous quarter. In contrast, growth in *Health care and social assistance* slowed to 0.1% from 0.2%.

In the March quarter 2026, the general government net operating balance improved by $1.3 billion since the December quarter to record a deficit of $0.4 billion. This was a modest improvement relative to the December quarter, reflecting a 4.5% decline in taxation revenue to $220.6 billion over the same period.

Total revenue in the March quarter was 5.8% higher than in the corresponding period a year earlier, including a 6.6% increase in taxation revenue. Meanwhile, total expenses rose by 5.9% compared with the March quarter 2025.

FIGURE 23
Australian Government Tax Receipts by Type
Seasonally adjusted, mil AUD



Source: ABS, Haver, KPMG

Taxes less subsidies on production imports rose by 0.6% in the March quarter 2026.

Taxes on production and imports remained flat at 0.0%, with declines in financial and capital transaction taxes, and motor vehicle taxes. This was partly offset by increases in international trade taxes and GST.

The fall in taxes on financial and capital transactions was driven by weaker stamp duty collections across most major states, while motor vehicle tax revenue declined in line with subdued car sales. By contrast, taxes on international trade increased, supported by higher tobacco imports, and stronger household consumption underpinned growth in GST collections.

Meanwhile, subsidies on production fell by 1.6%, driven by lower national general government subsidies due to weakness in fuel tax credits and the Building Skills and Capability program. This was partly offset by a rise in state and local general government subsidy payments, particularly for transport, water services, and major sporting events.

Long-term Australian government bond yields have risen in recent months, reflecting a reassessment of the outlook for inflation and monetary policy. The 10-year yield increased from 4.65% in March 2026 to 4.98% in May (the highest monthly average since July 2011) before moderating to 4.82% in June 2026.

Short-term yields have also moved higher alongside changes in policy expectations. The 3-year yield averaged 4.65% in April/May 2026, up from 4.27% in January before easing slightly to 4.46% in June.

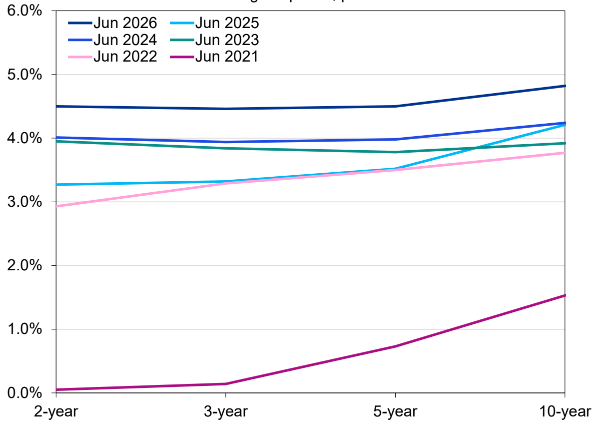
The yield curve has flattened, with the spread between 10-year and 3-year yields narrowing to below 40bpt since March, currently at 37bpt in June, down from around 50 to 90bpt in early 2026. This reflects a larger overall increase in short-term yields relative to long-term yields, as markets have repriced the near-term policy outlook while longer-term inflation expectations have remained more anchored.

The financial account recorded a surplus of $18.9 billion in the March quarter 2026, driven by net inflows of debt of $11.2 billion and net inflows of equity of $7.7 billion. The net inflows of debt indicate continued demand for Australian debt securities, contributing to capital inflows into Australia and supporting demand for government bonds.

FIGURE 24

Australian Treasury Bond Yield Curve

Average of period, per annum



Source: ABS, Haver, KPMG

Financial conditions

Understanding financial conditions requires analysis that goes beyond just the overall stance of monetary policy but rather needs to examine a broad set of indicators across various sectors and issues.

About the KPMG Financial Conditions Index

The *KPMG Financial Conditions Index* measures the state of financial conditions in Australia, not just for the overall economy but also for households and businesses. We assess financial conditions by examining a broad set of complementary indicators, as detailed in the table below. A significant deviation of an indicator from the average of the sample means that the financial conditions are more restrictive/expansionary.

An expansionary financial condition indicator (blue text) indicates that the greater that variable from its average, the more expansionary the financial conditions are. Conversely, a restrictive financial condition indicator (pink text) indicates that a larger deviation from the average corresponds to more restrictive conditions.

Blue dots show the latest readings, while pink dots show the average over the sample and the grey bars show the middle 50% of observations (the interquartile range).

Given the extensive data available, we assess financial conditions for households, businesses, and the overall economy by computing the first principal component for household finance variables, business finance variables, and all variables combined, respectively.

These indicators are transformed to annual growth terms (or annual changes for rate indicators such as interest rates or yields). All transformed series are then standardised to have a mean of zero and a standard deviation of one. Additionally, to ensure consistent interpretation, all restrictive variables are reversed.

Indicators of Financial Conditions, 2003 to 2026

		Min		Max
Household	Growth in new housing finance commitment (%, y/y)	-29.7	18.5	83.2
	Growth in new personal finance commitment (%, y/y)	-21.5	14.5	35.1
	Growth in housing credit (%, y/y)	3.0	7.3	21.9
	Growth in personal credit (%, y/y)	-12.9	4.5	16.1
	Discounted variable rates for owner-occupiers (%)	3.5	6.6	8.8
	Credit card standard rates (%)	16.0	21.0	21.0
	Growth in income spent on interest on dwellings (%, y/y)	-25.5	-2.3	108.1
	Growth in income spent on consumer debt interest (%, y/y)	-24.4	-0.8	34.9
Business	Growth in lease finance commitment (%, y/y)	-36.2	16.3	42.6
	Growth in commercial lending (%, y/y)	-7.1	7.6	44.9
	Growth in business credit (%, y/y)	1.1	8.1	15.6
	Non-financial 3yr A-rated bond yields (%)	0.7	5.1	8.7
	Non-financial 10yr A-rated bond yields (%)	1.5	5.5	9.0
	Non-financial 3yr BBB-rated bond yields (%)	1.2	5.4	10.8
	Non-financial 10yr BBB-rated bond yields (%)	2.4	5.8	12.3
Other Macro	Growth in government lending (%, y/y)	-43.0	8.0	178.0
	Growth in bond issued as a percentage of GDP (%)	-8.2	-6.9	28.0
	Growth in real trade-weighted index (%, y/y)	-19.9	9.2	29.3
	Growth in ASX 200 share price index (%, y/y)	-40.9	7.1	37.0
	Official cash rate (%)	0.1	4.1	7.2
	10-year government bond yields (%)	0.8	5.0	6.4

Source: ABS, RBA, S&P, KPMG

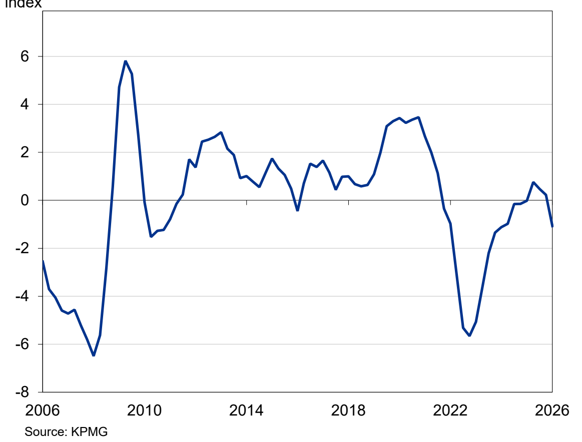
Australia's financial conditions have tightened

The *KPMG Financial Conditions Index (FCI)* deteriorated sharply in the March 2026 quarter, indicating that financial conditions have become more restrictive.

The FCI fell to -1.07pts, down from 0.23pts in the December quarter, returning to restrictive territory after a period of modestly supportive conditions from the June quarter 2025 to the December quarter 2025.

The tightening in overall financial conditions was largely driven by weaker business financial conditions, while household financial conditions, although easing, remained positive and helped to offset some of the overall pressure. The recent cash rate increases, together with expectations of further rises, have lifted borrowing costs, weighing on financing conditions for both households and businesses. Meanwhile, rising bond yields and an appreciating Australian dollar, along with higher energy prices pushing up inflation and uncertainty, have also added further pressure to financial conditions.

FIGURE 25
KPMG Financial Conditions Index



Source: KPMG

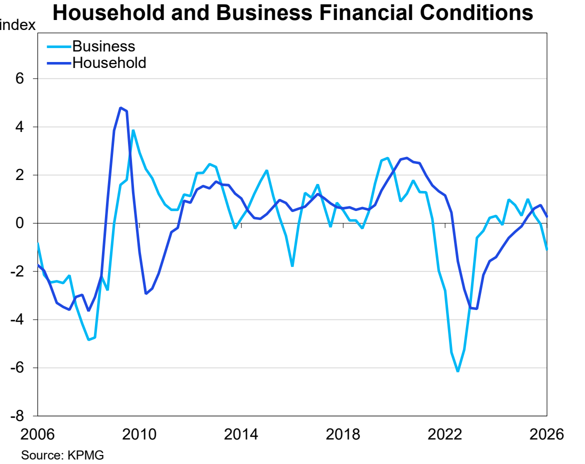
Household financial conditions remain positive but show signs of easing

Household financial conditions weakened in the March quarter, with the household FCI falling to 0.28pts from 0.76pts in December 2025. However, conditions remain positive and are still above the -0.13pts recorded a year earlier.

Although some of the earlier momentum has eased, household financial conditions remain in expansionary territory. This reflects continued support from household savings buffers, which have helped sustain incomes and spending. However, higher mortgage repayments following recent cash rate increases, together with rising fuel costs and weaker consumer sentiment, have begun to weigh on household cash flow and confidence, moderating the strength in household financial conditions.

Nevertheless, higher interest rate, elevated cost of living following geopolitical tensions, and a softening labour market are looking to place further pressure on household financial conditions over 2026.

FIGURE 26
Household and Business Financial Conditions



Source: KPMG

Business financial conditions remain weak as pressures intensify

The index remains in negative territory in the March quarter at -1.08pts, continuing the decline from -0.04pts observed in the December quarter 2025.

This persistent weakness reflects the impact of higher borrowing costs, which have weighed on business financing conditions and investment decisions. At the same time, increased uncertainty has reduced business confidence and risk appetite, leading firms to adopt a more cautious approach to spending and business expansions. As a result, tighter financial conditions have continued to weigh on overall business activity, leaving the near-term outlook weaker.

03

Forecasts

Global and domestic forecasts

GLOBAL	GDP Growth				Unemployment Rate				Inflation			
	2024 (a)	2025 (a)	2026 (f)	2027(f)	2024 (a)	2025 (a)	2026 (f)	2027(f)	2024 (a)	2025 (a)	2026 (f)	2027(f)
World*	3.3%	3.4%	3.0%	3.3%	4.5%	4.4%	4.5%	4.5%	4.7%	3.8%	4.8%	4.2%
Euro Area	0.9%	1.5%	0.3%	1.2%	6.4%	6.3%	6.3%	6.2%	2.4%	2.1%	3.1%	2.3%
US	2.8%	2.1%	2.2%	2.2%	4.0%	4.3%	4.3%	4.2%	3.0%	2.7%	3.6%	2.6%
China	5.0%	5.0%	4.7%	4.7%	5.1%	5.1%	5.2%	5.2%	0.2%	0.0%	1.2%	1.5%
Japan	-0.2%	1.1%	0.6%	0.5%	2.6%	2.5%	2.6%	2.4%	2.7%	3.2%	2.6%	3.3%
Indonesia	5.0%	5.1%	5.0%	4.9%	4.9%	4.8%	4.9%	4.8%	2.3%	1.9%	3.5%	3.4%
Malaysia	5.2%	5.2%	4.5%	4.2%	3.2%	3.0%	2.9%	2.9%	1.8%	1.4%	2.4%	2.4%
N. Zealand	-0.3%	0.5%	1.5%	2.6%	4.8%	5.3%	5.1%	4.8%	2.9%	2.8%	3.6%	2.2%
Philippines	5.7%	4.4%	3.6%	5.8%	3.8%	4.2%	4.8%	4.1%	3.2%	1.7%	6.4%	4.6%
Singapore	5.3%	5.0%	3.5%	2.3%	2.0%	2.0%	2.1%	2.0%	2.4%	0.9%	2.8%	3.7%
S. Korea	2.0%	1.0%	2.6%	1.6%	2.8%	2.8%	3.0%	3.2%	2.3%	2.1%	2.9%	2.2%
Taiwan	5.3%	8.8%	10.1%	3.3%	3.4%	3.3%	3.3%	3.4%	2.2%	1.7%	2.1%	2.6%
Thailand	2.9%	2.4%	1.9%	1.6%	1.0%	0.8%	1.0%	1.1%	0.4%	-0.1%	2.7%	2.5%
Vietnam	7.0%	7.9%	7.2%	7.4%	1.6%	1.5%	1.5%	1.4%	3.6%	3.3%	5.3%	4.4%

Note: Average percent change from previous calendar year for GDP growth and inflation; average unemployment rate. *GDP based on Purchasing Power Parity

AUSTRALIA	Q/Q Growth			Y/Y Growth			
	Q1-26 (a)	Q2-26 (f)	Q3-26 (f)	2025 (a)	2026 (f)	2027 (f)	2028 (f)
GDP and Components							
Consumption	0.5%	0.5%	0.1%	2.5%	1.5%	1.6%	1.9%
Business investment	6.0%	0.5%	0.4%	4.0%	7.5%	1.9%	2.3%
Housing investment	-0.5%	0.8%	-0.1%	6.4%	0.0%	0.2%	1.7%
Government	0.0%	0.2%	0.7%	2.4%	1.6%	2.6%	2.5%
Exports	-1.1%	0.7%	0.8%	5.2%	1.3%	3.4%	3.6%
Imports	2.1%	1.5%	1.0%	6.7%	5.7%	4.1%	4.5%
GDP	0.3%	0.3%	0.3%	2.5%	1.2%	1.6%	1.9%
Inflation and Rates							
Headline CPI*	1.2%	1.2%	0.7%	3.7%	4.0%	3.0%	2.7%
RBA cash rate*	4.10%	4.35%	4.60%	3.60%	4.60%	4.35%	4.35%
10-year government bond*	4.97%	4.73%	4.75%	4.74%	4.77%	4.88%	4.96%
AUD/USD*	0.69	0.69	0.71	0.67	0.71	0.71	0.71
Labour Market							
Employment	0.6%	0.5%	0.5%	1.1%	2.0%	1.8%	1.8%
Unemployment rate*	4.2%	4.2%	4.3%	4.3%	4.4%	4.7%	4.8%
WPI	0.8%	0.8%	0.8%	3.4%	3.3%	3.3%	3.1%

*Values at end of period

Industry growth forecasts

Since publication of the previous Quarterly Economic Outlook published in early this year the ABS has revised down GVA for the *Agriculture, forestry & fishing* industry in FY2025.

The *Agriculture, forestry & fishing industry* will be pressured by the impacts of the Iran war, particularly if the conflict continues for an extended period and diesel and fertilizer costs remain higher for longer. The forecast for the Mining industry has been revised down. This reflects the impact of the Iran conflict and a general weaker economic demand for commodity.

Conditions for the *Manufacturing* industry remain difficult. Higher input costs, elevated energy prices and a relatively strong Australian dollar environment continue to weigh on competitiveness. As a trade-exposed sector, manufacturing remains particularly vulnerable to global cost pressures and shifts in relative prices. Reflecting these challenges, we continue to project that manufacturing GVA will contract over the next two years and under-perform growth in the broader economy.

We continue to expect that industries exposed to government spending, including *Public administration & safety and Health care & social assistance* will record faster GVA growth than the economy as a whole. GVA growth in *the Education & training* industry is expected to grow modestly in FY2026 and to under-perform the economy as a whole over the forecast horizon.

GVA growth in the *Retail trade* industry has been very weak over the past two years. KPMG's forecast has GVA for the *Retail trade* industry growing in line with the recovery in household consumption. GVA growth in the *Accommodation & food services* industry is also expected to grow in line to the *Retail trade* industry, reflecting its susceptibility to cost pressures that stifle discretionary consumption spending and hold back growth in tourism expenditures

About the KPMG-CGE Model

The following industry Gross Value Added (GVA) forecasts have been prepared using a combination of aggregate economic forecasts developed in KPMG's macro-econometric model (and presented in the previous table); which are then applied to our KPMG-CGE model which disaggregates the national forecasts on a theoretically consistent basis into 20 industry sectors that match the ABS ANZSIC industry classifications.

INDUSTRY GVA	FY2025 (a)	FY2026 (f)	FY2027 (f)	FY2028(f)
Agriculture, forestry & fishing	5.1%	4.3%	1.7%	1.9%
Mining	-1.0%	3.1%	2.5%	4.3%
Manufacturing	-2.3%	-0.1%	-0.6%	0.1%
Electricity, gas, water & waste services	3.7%	2.5%	0.9%	1.6%
Construction	0.3%	2.1%	1.2%	1.9%
Wholesale trade	0.1%	2.6%	0.9%	1.2%
Retail trade	0.7%	2.6%	1.0%	1.3%
Accommodation & food services	-0.5%	2.0%	0.1%	0.6%
Transport, postal & warehousing	2.8%	3.7%	1.1%	1.4%
Information media & telecommunications	3.1%	4.1%	1.1%	1.3%
Financial & insurance services	3.4%	4.0%	1.2%	1.6%
Rental, hiring & real estate services	1.7%	2.5%	0.8%	1.4%
Ownership of dwellings	1.5%	2.0%	0.9%	1.3%
Professional, scientific & technical services	-0.9%	0.1%	-0.2%	0.8%
Administrative & support services	1.4%	2.5%	0.7%	1.3%
Public administration & safety	3.4%	3.9%	1.7%	2.0%
Education & training	0.8%	1.8%	0.2%	0.7%
Health care & social assistance	3.2%	3.1%	1.3%	1.8%
Arts & recreation services	3.6%	2.6%	0.8%	1.3%
Other services	-0.8%	2.3%	0.8%	1.6%

*Note: Annual Growth in Real Gross Value Added, measured as the sum of the 4 quarters ended on June 30 of year *t* relative to the sum of the 4 quarters ended on June 30 of year *t-1*.

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