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Secretary to the Treasury

Economic Policy Amid Global Uncertainty

Post-Budget economic briefing*

Address to the Australian Business Economists

28 May 2025

Thank you Besa.

I begin today by acknowledging the Traditional Custodians of the land on which we are meeting, the Gadigal people of the Eora Nation, and I acknowledge their ongoing connection to Country.

I pay my respects to their Elders – past and present – and extend my respect to any First Nations people who are here with us today.

It's a pleasure to be with the Australian Business Economists (ABE) for the annual post-Budget address.

Three key themes have dominated my previous addresses to the ABE:

- Global trends and their impacts on Australia.
- Structural forces such as demographics, climate change and secular declines in productivity.
- Fiscal sustainability.

I will again touch on these constants today. However, this presentation comes not when the Budget is newly printed, but instead with some delay due to the election and in the wake of elevated global uncertainty.

Economic forecasters like to add a rider to their forecasts, that there is more than the usual degree of uncertainty surrounding the outlook.

It may be time to stop saying that and accept that for the foreseeable future the world will be characterised by a persistent high level of uncertainty, a level not experienced for decades.

* I would like to express my appreciation to Katrina Di Marco, Shane Johnson and Matthew Rudd for their assistance in preparing this address.

Current global conditions make policy trade-offs starker – they demand evidence driven approaches. The margin for error is smaller and the need for insurance against damaging outcomes is higher.

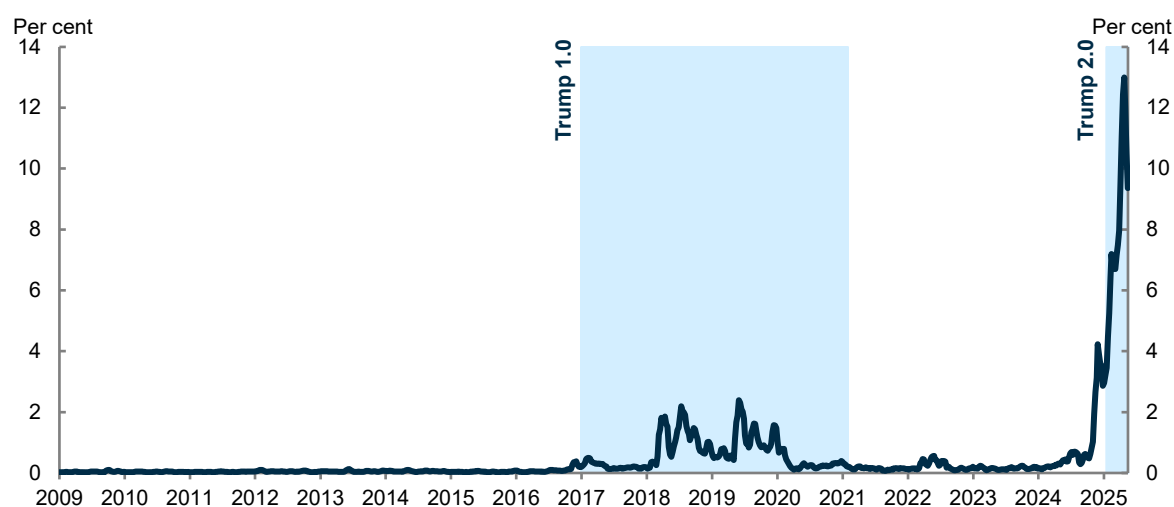
I'll start with observations about recent economic developments, discuss a new international paradigm, outline how countries are responding to these developments, before turning to policy opportunities more broadly with a focus on productivity and fiscal policy.

Recent economic developments

The economic update for Pre-election Economic and Fiscal Outlook (PEFO) was finalised on 31 March. The tariffs announced by the United States (US) President on 3 April were more substantial than expected, and since this time, markets have experienced unusually high levels of volatility. Initially, the 90-day delay of 'reciprocal' tariffs on all countries other than China calmed markets a little (see Chart 1).

The subsequent ratcheting of tariff levels between China and the US and more recent de-escalation serves as a reminder that both have dependencies and vulnerabilities, and tension will remain for the foreseeable future.¹

Chart 1: Trade uncertainty index



Note: 21-day rolling average. Bloomberg Economics Trade Policy Uncertainty (TPU) Index is aligned with the indexes developed by Baker, Bloom & Davis and Caldara et al., showing similar historical changes since 2018.

Source: Bloomberg Economic Global Trade Policy Uncertainty Daily

¹ On 12 May, US tariffs were reduced from 145 per cent to 30 per cent (on top of sectoral tariffs and fentanyl related tariffs) and Chinese tariffs on US goods were reduced to 10 per cent.

China has a lot to lose should exports to the US be significantly curtailed. It is estimated that 16 million people work in sectors that export to the US.²

The US also has a lot to lose if they cannot access Chinese goods, especially in the near term, with processed critical minerals sitting near the top of the list.

The US heavily relies on Chinese imports that are not easily replaceable or producible domestically without incurring significant costs. Adam Posen has gone as far as to say that this dependency makes the US more vulnerable to trade disruptions than China, which can more readily find alternative markets for its exports.³

Unsurprisingly, these developments have led to a downgrade to the global outlook.

The International Monetary Fund (IMF) recently downgraded global growth for 2025 to 2.8 per cent, from 3.3 per cent. The largest downgrades to the outlook were for the US and China, which were downgraded by 0.9 and 0.6 percentage points respectively.

The impact of the downgrades to Chinese growth on global growth will be larger than the impact of downgrades to US growth.

Outside of the years affected by COVID-19, China has contributed more to world growth than the G7 since 2006. And more than the US since 2001.

We expect lower demand for Australia's exports (particularly from China) to weaken domestic growth. This may be exacerbated by lower consumption and investment as households and businesses react to the heightened uncertainty and the disruption to supply chains.

A weaker economy would be expected to flow through to a weaker labour market and lower wage growth.

There are offsetting impacts on domestic inflation, with the net effect likely to reduce inflation.

While tariffs present a global inflationary shock as supply chains are reconfigured, low-cost output from China will be disinflationary as China diverts its trade. Movements in the exchange rate and oil prices are also shaping outcomes. Oil prices are currently well below what we assumed in PEFO.

Any significant disruptions to financial markets would further jeopardise the growth outlook.

² Yang and Chen (2025) Goldman Sachs Economics Research - China: Labor market implications from heightened US tariffs.

³ Posen (2025) [Trade Wars Are Easy to Lose: Beijing Has Escalation Dominance in the U.S. China Tariff Fight](#).

The tariff announcements have ushered in volatility in bond markets, pushing long-dated US Treasury yields higher. More recently, bond market volatility reflects anxiety over the US fiscal outlook and rising deficits, as the spending and tax bill introduced by the Trump administration is projected to add over US\$3 trillion to the national deficit in the next decade.

In light of the heightened uncertainty, we are increasingly relying on scenario analysis to test policy positions and understand the risks.

We have assessed a range of scenarios on how current US trade policy could evolve, two of which were presented in the 2025-26 Budget. A key takeaway from these scenarios is that an increase in tariffs is likely to lead to a modest reduction in Australia's real GDP over time.

Given our limited trade flows with the US, the indirect impact is nearly four times as large as the direct effect.⁴

However, the impacts of uncertainty regarding policy directions, outcomes or asset values have the potential to be more damaging than tariffs.

To illustrate this, we have modelled a scenario where both tariffs and investor uncertainty affect financial market conditions. Not surprisingly, output falls by even more under this scenario for all countries, driven by lower investment.⁵

We have also modelled a scenario where risk in the US arises due to policy choices. In this case output rises in Australia and China, reflecting their increased attractiveness as an investment destination compared to the US.

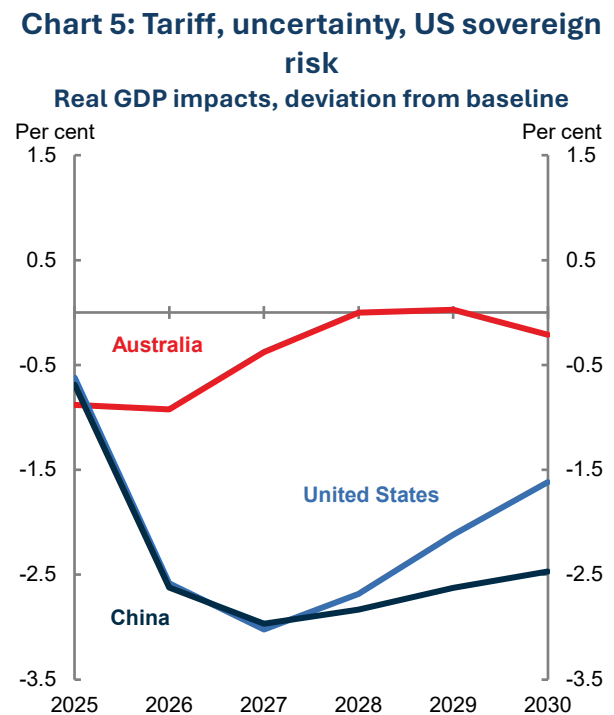
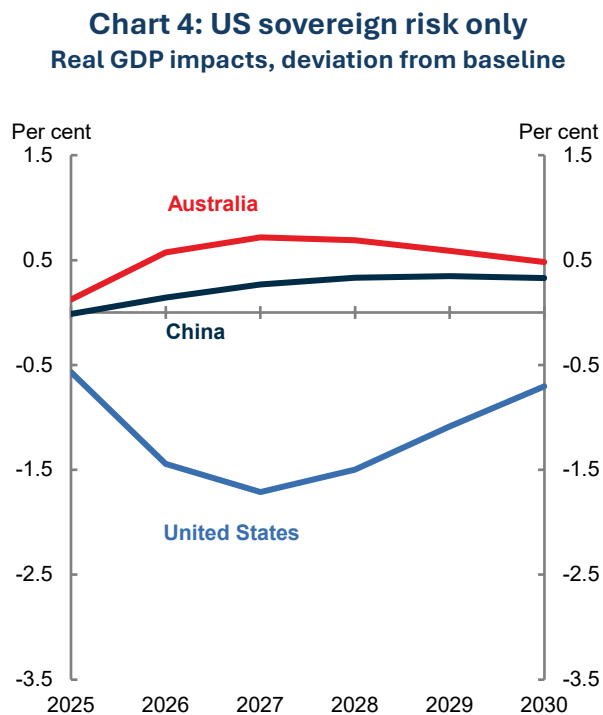
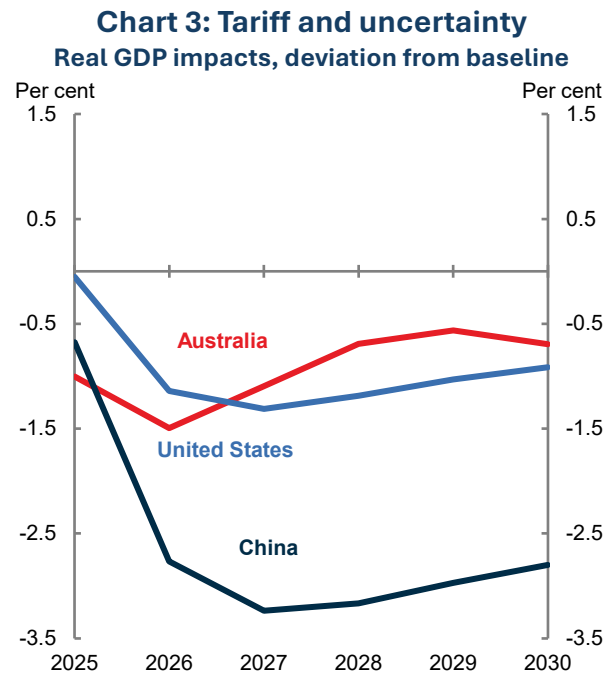
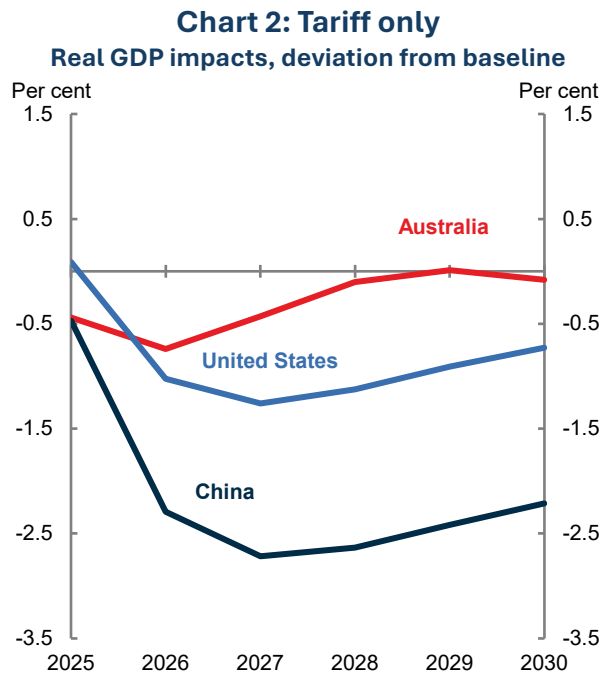
Lastly, we assessed the cumulated impacts of trade policy, heightened uncertainty and increased risk in the US. The net effect of this scenario is a decline in output but not to the same extent as the scenario where risk in the US does not change.

The importance of policy that improves Australia's relative attractiveness as an investment destination is illustrated through these scenarios (see Charts 2 to 5).

⁴ Treasury (2025) [Budget Paper No. 1](#), pp.38-39

⁵ An increase in uncertainty leads to a decline in business investment as investors seek safer alternatives. This in turn reduces demand for investment goods, such as machinery and equipment, which are often imported. The aggregate economic impact of rising uncertainty and tariffs varies across countries, largely due to differences in the shares of investment goods in GDP. Australia's GDP declines relative to that of the US for a combination of factors including the direct effect of lower investment, the spillover effects of lower demand for investment good exports from some of our largest trading partners, and the economy's relatively rapid adjustment to the increased uncertainty.

Trade scenarios



Source: Treasury analysis using G-Cubed

A new international paradigm

The US administration has made it clearer that it intends to reshape the global economic and political order to further its interests. In doing so, our key security partner and the world's dominant financial power has pitted itself against China, the world's dominant manufacturing power, and a country with significant influence on our prosperity (see Chart 6).

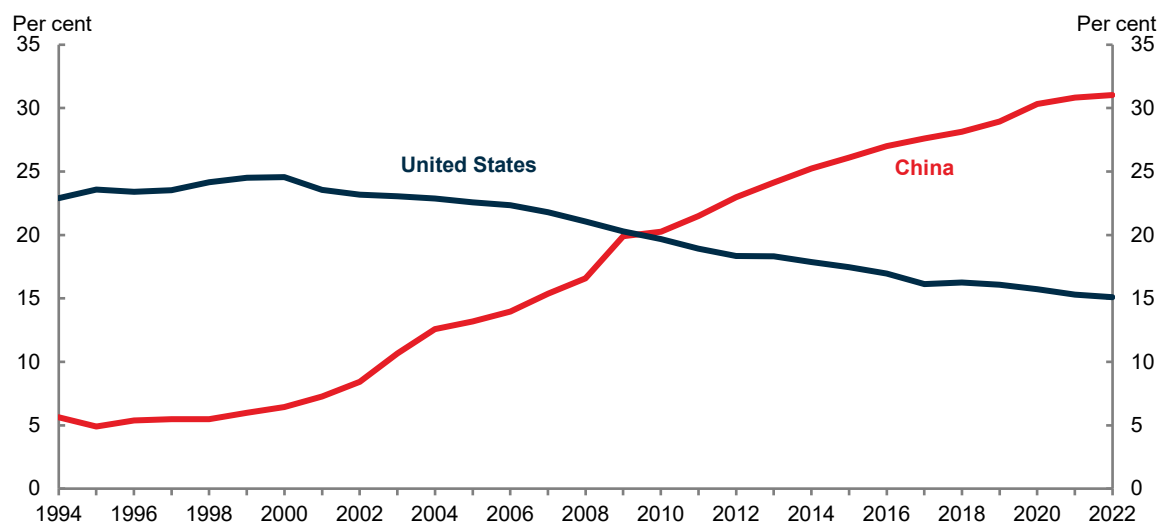
However, the US has gone further than sharpening the contest with China, it has told the rest of the world that it will more robustly pursue its own interests in all domains and expect others to lift their effort on peace and security. These actions reflect an underlying belief that the rules, norms and institutions the US sponsored no longer serve its interests.

Australian policy will have to adjust this reality.

Concerns that China is hollowing out US manufacturing through unfair trade and industrial practices have been present for decades and are largely bipartisan.

Transition memos from the end of the Bush administration highlight the growing concerns of China's economic ascendancy less than a decade after joining the World Trade Organisation (WTO).⁶

Chart 6: Shares of global manufacturing (value added)



Source: United Nations Industrial Development Organisation

⁶ Hadley Ed (2016) Hand-off: The Foreign Policy George W Bush passed to Barack Obama

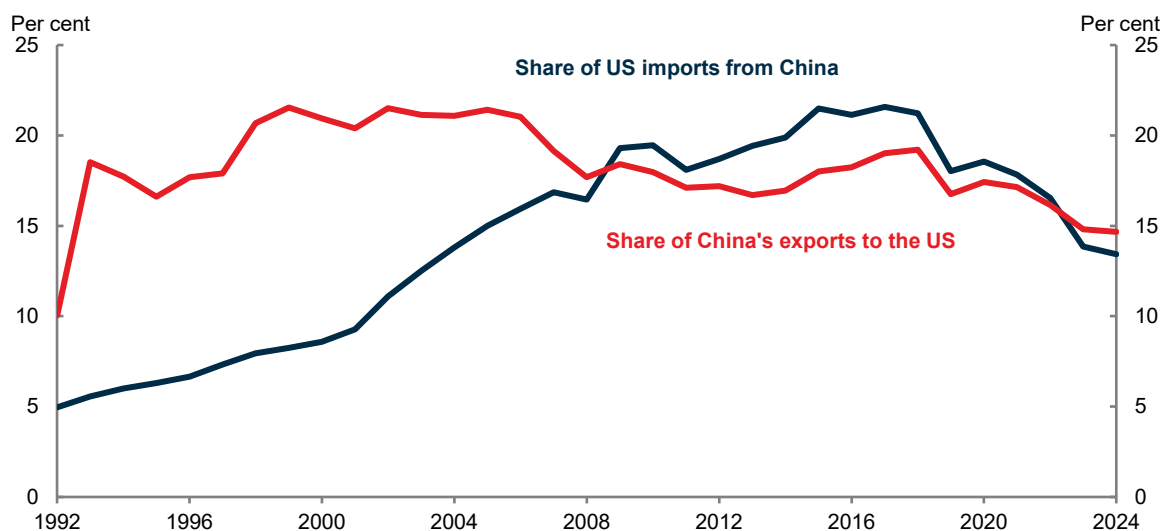
As China's share of global manufacturing and output continued to grow, so did the outward signs of strategic competition. By 2016, the Trans-Pacific Partnership (TPP) was unashamedly a US plan designed to counterbalance China's growing economic weight in the region.⁷

During the first Trump administration more direct US measures were put in place, including tariffs.

Since this time, US imports from China have steadily declined from their peak of 21.6 per cent of total imports in 2017 to 13.4 per cent in 2024.

By 2024, at 14.7 per cent, the share of China's exports going to the US were at their lowest level since 1992 (see Chart 7).

Chart 7: US-China direct trade relationship



Source: International Monetary Fund and WIND

Beyond the sharpening of US and Chinese strategic competition is the stark re-emergence of long-standing tensions around the world.

Russia's illegal invasion of Ukraine has been a critical turning point in European strategic and economic policy.

Underscoring this reality, the Swedish and French Governments have produced brochures informing their citizens about how to prepare for a variety of threats, including armed conflict.

And in the last year, conscription has been a topic of genuine political debate in Germany and Poland.

⁷ Obama (2016) [President Obama: The TPP would let America, not China, lead the way on global trade](#)

The challenges associated with familiar structures becoming more fragile extends beyond the international arena.

Within nation-states, electorates and mass communication channels have become more fractured and polarised. Nationalism is proving to be a more enduring, motivating and powerful force than globalisation.⁸

The pandemic and conflict-driven energy and inflation shocks, along with the consequent monetary tightening, amplified frustrations with the cost of living and inequality.

In many places, this has manifested in populism and a wave of anti-incumbency.⁹

Consensus-building for new policy has become more challenging in democratic societies. And it has made it more difficult to anticipate how governments might respond to evolving circumstances.

In some countries, we are seeing the institutions of democracy and even the judiciary under pressure.

Fortunately for Australia, our institutions supporting democracy, such as the Australian Electoral Commission, continue their exemplary performance and they enjoy widespread public support and trust.

How are countries responding to global uncertainty and fragmentation?

We see three key trends in the policy choices by governments in response to global uncertainty and fragmentation: building resilience, trade and economic diversification and investment in deterrence.

Building resilience

The most effective strategy to build resilience is to raise the productive capacity of the economy through reforms.

In Europe, last September, Mario Draghi presented a report to the European Commission aiming to build economic resilience by removing barriers to their internal market.¹⁰

In Canada, a key focus is on removing all federal barriers to interprovincial trade, which could lower prices by up to 15 per cent.

⁸ See Vinjamuri in Chatham House (2025), [The fracturing of the US-led liberal international order](#)

⁹ Australian Strategic Policy Institute (2025), [In 2024, a global anti-incumbent election wave | The Strategist](#); IPSOS (2025) [The factors driving anti-incumbent anger](#)

¹⁰ This identified three priorities: closing the innovation gap, a comprehensive plan for decarbonisation and competitiveness, and increasing security and reducing dependencies see European Commission (2024) [The Draghi report on EU competitiveness](#)

To support investment, the Canadian Government has also committed to ‘one project, one review’ by eliminating duplicate federal requirements for projects of national significance, already assessed by provincial governments.

The UK Government has accelerated their growth mission to move ‘faster and further’ on domestic reforms. Recently introduced reforms to planning and infrastructure such as accelerated environmental approvals, incentives to support new electricity connections and reducing consultations required for planning approvals have the potential to be significant.

Trade and economic diversification

Larger countries can, even if inefficiently and imperfectly, pursue a strategy of self-reliance and strategic autonomy. For most other countries, when large countries raise barriers, it is not in our self-interest to respond by also raising barriers.

Instead, strength will be found in removing barriers to trade and increasing diversification.

Countries and trading blocks are moving quickly to enhance and strike new trade agreements. In recent months Canada, the EU, Germany and the UK have all announced renewed efforts to seek new trade partnerships, in particular with those in our region.

The EU has committed to eliminating its dependency on Russian gas by 2027. Already dependence is down from 45 per cent of imports in 2021 to a projected 13 per cent this year.

Japan is securing critical mineral supplies through agreements with Australia and India to mitigate semiconductor supply chain risks.

Investment in deterrence

The third response is in support of deterrence and includes defence investment and national security agreements and policy.

There have been commitments to increase defence investment around the world including from Japan, Canada, the UK, Sweden and New Zealand.¹¹

Japan, Canada and New Zealand have all committed to increase spending to 2 per cent of GDP over the coming years while the UK and Sweden have gone further.

¹¹ [Japan](#), [Canada](#), [United Kingdom](#), [Sweden](#) and [New Zealand](#).

In 2024, German spending on defence had risen to nearly 2 per cent of GDP for the first time in three decades. This is set to increase further with new European¹² and domestic laws that relax fiscal rules to exempt spending on defence and security from borrowing constraints.

In addition to increases in defence expenditure, countries are moving to strengthen defence agreements around cooperation, weapons production and other security arrangements.

Australia's response

Australia has also been responding to global developments.

Resilience

Lifting both the rate and stability of productivity growth is the most salient way we can build resilience. I will shortly return to this topic.

The National Interest Framework and the Economic Resilience and Security Stream in particular, aim to ensure the deployment of limited public resources are evidence-based and focused on those areas where the sector is critical, the supply chain is vulnerable and there are limits on the ability of the sector to self-insure.

Importantly, successful economic security policy needs to combine strategic government investment with market-based mechanisms, to ensure economic growth and public trust.¹³

Diversification

Responding to tariffs or trade restrictions with similar measures will only make matters worse. We need to make it easier for business to find new markets.

The Government has committed to recommencing negotiations with the European Union on a Free Trade Agreement and is looking at ways to reinforce and expand the existing architecture such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership.

Through Treasury's stakeholder engagement we have already heard of firms finding new markets to mitigate tariff exposure. We have seen during trade tensions with China that firms were able to reorient their exports although not without impacts on some suppliers and communities.

¹² The recently launched White Paper [ReArm Europe/Readiness 2030](#) has sought to boost defence spending by around 800 million euros in EU member states, largely by allowing member states to activate a 'national escape clause' to allow them to increase spending on defence and not breach EU fiscal rules.

¹³ Furman (2025), [The Post-Neoliberal Delusion | Foreign Affairs](#)

There is also the potential to benefit, as risks mount in other markets, there may be a premium for markets such as Australia with its stable policy settings.

Deterrence

Deterrence requires both capability and a strong commitment to readiness and resilience in concert with our partners in the region.

Defence expenditure is currently 2 per cent of GDP. The Government will increase defence spending which is set to exceed \$100 billion annually and 2.4 per cent of GDP by 2033-34.

Investment in defence in Australia needs to continue to adapt to Australia's economic structure. Compared to some countries our industrial base is narrow, representing the strength of resources, agriculture and services sectors.

These sectors are crucial to our economic strength and resilience, and unnecessarily diverting resources away from them to sectors where our comparative advantage is weak would only degrade our resilience and productivity. Especially in an economy near full employment.

The mix of procurement, sovereign capability and sustainment has to be considered carefully in Australia. The 2026 National Defence Statement will need to grapple with these challenges.

Resilience through productivity

When we think about the goals of macroeconomic policy, we tend to focus on three objectives: full employment, low and stable inflation and higher living standards through productivity growth.

Over the past 3 decades, we have made substantial progress in maintaining low and stable inflation through the institutional arrangements that underpin the RBA. Recent Government reforms will further strengthen these arrangements. More recently we have made a significant step forward in moving toward and sustaining the economy at full employment.

But finding ways to improve productivity growth has proved elusive over the past two decades. Australia's 20-year average productivity growth has declined from 1.8 per cent to 0.8 per cent over that period.

Australia is not alone in facing these challenges. Nor the challenges posed by demographic shifts, the cost of the energy transition, increased pressure on defence spending, and diminishing returns to existing technologies. These all make it more difficult to generate more outputs with the same stock of inputs.

Thirty years ago, the Hilmer reforms aimed to boost the productivity of our non-traded sector – electricity, telecommunications and gas – that were often dominated by government and holding back the newly exposed traded sector that needed them as inputs.

Improving competition and the operation of markets drove productivity growth and lifted real wages.

Yet the core goal of the Hilmer reforms, developing a single national market to allow Australia to compete in the world, remains unfinished.

Even though the context has changed, such reforms are still needed today.

To this end, the Government has asked the Productivity Commission (PC) to map out potential reforms to boost productivity under the following five pillars:

- Creating a more dynamic and resilient economy.
- Investing in cheaper, cleaner energy and the net zero transformation.
- Building a skilled and adaptable workforce.
- Harnessing data and digital technology.
- Delivering quality care more efficiently.

The PC recently opened a consultation portal on its website which I encourage you all to use and provide feedback.

But it's also worth considering some of the reforms already underway in these five areas.

Dynamic markets

The role for competition

Competition is the main way of lifting productivity over time, by spurring businesses to make more with less.

Professor Carl Shapiro defines competition as ‘a process of rivalry that incentivizes businesses to offer lower prices, improve wages and working conditions, enhance quality and resiliency, innovate, and expand choice, among many other benefits.’¹⁴

Competitive markets help ensure that productivity gains – when they do occur – are passed on to workers as higher wages and to consumers through lower prices and better quality and service.

¹⁴ Shapiro (2024), [*Using Economics To Diagnose a Lessening of Competition*](#)

Competition also unpicks economic rent and privilege ensuring a fairer distribution of resources. This means the gains from economic growth are shared more widely – and more quickly – across the community.

Unlike boosting productivity by spending more on capital or education and training, enhancing competition shouldn't cost the budget.

In fact, competition reforms improve the fiscal position by permanently lifting incomes (boosting tax revenue) without requiring ongoing funding.

National Competition Policy

This concept underpins the Government's \$900 million National Productivity Fund.

The states are paid on delivery for reforms that boost the national economy which the Commonwealth benefits from in the form of higher taxes, offsetting the cost of the Fund.

There are some other unique features that make National Competition Policy a successful vehicle for the national reform effort needed to lift productivity.

Reforms are jointly agreed by Treasurers to ensure they have some political backing. Guidelines reflect lessons learned by the more successful states and previous reviews, so everyone knows what best practice is and how to get there.

The National Competition Council will also be revived to independently assess and report on state efforts for payment.

Road user charging

The High Court's 2023 decision in *Vanderstock*¹⁵ raises important questions about our federal fiscal balance and road pricing reform.

And it is catalysing a debate about how the Commonwealth and the states might deliver and maintain road infrastructure into the future.

Since the Harper review recommendations, governments have been trying to deliver reforms that treat roads like an economic asset, where users are charged for the damage they do, and roads are built and maintained where they are most needed.

Despite such efforts, road funding and charging today remains largely indistinguishable from how it was done over 30 years ago, despite nearly all other public utilities being subject to efficiency reforms.

New technologies, the shift away from fossil fuels, and the need for a resilient and productive logistics system, may present us with an opportunity.

¹⁵ *Vanderstock v Victoria* (2023) HCA 30

This includes an opportunity to encourage more efficient and productive use of roads, where externalities, such as damage and congestion are appropriately priced.

Climate and energy

The climate and energy transition brings both costs and opportunities.

Pursuing a least-cost approach to reducing emissions will be a key productivity challenge for Australia.

As the Government looks towards setting a 2035 emissions reduction target, we have an opportunity to consider how market mechanisms can help us achieve it in a way that supports strong growth.

The Safeguard Mechanism is an efficient market mechanism with which to reduce emissions. The mechanism is due for review in 2026–27. As highlighted by the PC in its 2023, 5-year review, reform of the Safeguard Mechanism presents an opportunity to expand and improve its effectiveness.

Given the cost of carbon emissions is undervalued by markets, there will be underinvestment in reducing emissions. But this is not an unmovable constraint.

The Government can support investments that would efficiently reduce emissions consistent with our targets.

Getting regulatory settings right: the National Electricity Market

Australia's energy transition is occurring quickly – with renewable generation now making up over 40 per cent of our electricity supply in the National Electricity Market (NEM).

Progress is needed to ensure reliable and affordable energy for consumers and business – ageing and increasingly unreliable coal powered generators need to be replaced with new generation while balancing reliability with the impact on prices.

Replacing coal will require a mix of technologies – from variable renewables to provide bulk supply; gas, hydro and battery storage to preserve the reliability and security of our grid; and transmission to open up new sources of generation while increasing resilience through greater interconnection.

The NEM was designed for dispatchable, centralised generation. As it transitions towards a variable renewable based grid, stronger incentives will be needed for the firm generation, storage and distributed energy resources needed to provide services like inertia, frequency control, and flexible supply and demand.

Designing a framework that provides the long-term signals for this investment is the key objective of the independent review into the NEM wholesale market settings due in late 2025.

Getting regulatory settings right: environmental approvals

The Government has re-committed to reforming Australia's national environmental law to deliver better environmental protections and faster, clearer decisions for business.

Environmental approvals are about managing environmental risks, but they also require navigating complex trade-offs across other economic, environmental and social domains.

This requires good evidence and good frameworks to make sensible decisions.

We must be alert to the trap of letting poor analysis make those trade-offs look simpler than they are.¹⁶

Skilled workforce

In recent years five factors define the labour market:

- Record participation.
- Low unemployment.
- Addressing wage relativities for feminised industries.
- High migration.
- Slowing dynamism or job matching.

I'll focus my discussion today on dynamism and mobility.

Mobility

National occupational licensing would remove unnecessary barriers to labour mobility by enabling workers to work seamlessly across state and territory borders without reapplying for a separate licence or paying additional fees.

The Government is committed to implementing national licensing for electrical trades, which could be addressed through the National Competition Policy framework. Working with the states, this could mean licensed electricians could work anywhere in the country.

If successful, this approach could be a template for other trades to follow. Broader reforms to occupational licensing could boost GDP by up to \$10 billion.¹⁷

Work is underway to develop a National Screening Check for workers in the care economy to improve labour mobility.

¹⁶ <https://www.piie.com/sites/default/files/2024-09/furman2024-09-27.pdf>

¹⁷ Productivity Commission (2024) *National Competition Policy: modelling proposed reforms*

The Government has announced an intention to ban non-compete clauses for low- and middle-income workers beginning 2027. This responds to international and domestic evidence that these clauses are hampering job mobility and constraining the wages of affected workers. It follows PC modelling demonstrating a significant productivity gain from reform in this area.

Housing

Australia's housing shortage has significant implications for productivity and long-term economic growth.

Limited supply of affordable and well-located housing imposes higher costs on workers and reduces their ability to pursue jobs that are higher paying or that better match their skills. This reduces labour market efficiency and adaptability.

High housing costs also curtail household disposable income and concentrate household capital investment in the housing sector.

This reduces Australia's aggregate productivity growth, as construction productivity remains low and the concentration of capital investment in housing crowds out investment in higher-productivity industries.

This shortage is driven by planning constraints, input constraints (skilled labour, materials and infrastructure ready land), and poor sector productivity.

Increasing housing supply is crucial to improving affordability.

Technology adoption

The potential benefits of technology adoption are diverse, including improvements in productivity, economic and social inclusion, and living standards.

Several studies have shown that tech adoption and employing tech workers can have a significant positive impact on productivity - enabling automation, improving communication, and fostering a more efficient work environment.¹⁸

Some early Treasury analysis supports these findings indicating firms that have recently increased their share of tech workers are more productive, typically paying higher wages to their employees.

¹⁸ See for example Bartel et al (2007) *How Does Information Technology Affect Productivity*, Borland and Coelli (2023) *The Australian labour market and IT-enabled technological change*

Innovation

Many Australian businesses, particularly small businesses, are falling behind in the adoption of frontier technologies compared with other countries. As an example, Australia ranked in the 15th percentile among OECD countries for Artificial Intelligence (AI) adoption in 2020.

Globally, AI is moving more into the mainstream – this brings into sharper focus important questions around the benefits and potential harms.

While this technology comes with risks, it also comes with immense opportunities - and it's important Australia is not left behind.

There are a number of policy settings that can help households and businesses overcome challenges to adopting new technologies.

Improving competition will be key. As will be ensuring our regulatory settings are fit-for-purpose.

In this regard, it will be important that, wherever possible, we leverage existing technology-neutral laws and regulations to protect consumers and address clear harms – this provides certainty which will support innovation and more rapid adoption.

Care economy

At the Commonwealth level health care, aged care, disability support, and childcare are all growing faster than GDP – notwithstanding the significant efforts that have already been made to reduce spending growth in NDIS and aged care.

The state and territory governments face similar challenges especially in health care.

This is a significant productivity challenge.

At the outset it is difficult to measure productivity in these sectors but there have been some valuable insights generated through careful analysis.

The PC has looked at measuring patient outcomes, rather than delivery of care outputs, as a better way of capturing how value is created in the health and care sectors.

On this basis, productivity in the sector grew at 3 per cent per annum over the period 2011–12 to 2017–18 and Australia's healthcare sector is one of the most productive in the world.

But these productivity gains were not universal. Big gains were made from advances in saving lives but fewer in improving quality of life.

Some of our current funding models may create barriers to productivity growth.

For example, many government services are funded on a fee for service model. Providers are therefore paid based on the amount of activity they perform – such as amount of time spent with a patient – not on outcomes, or prevention.

We also need to make sure contributions to the cost of care, from those who can afford to make a contribution, are appropriate whilst still maintaining the principle of universal access.

The Government's reforms in aged care are a good example.

These reforms have improved the operation of the market by introducing price signals and user pays. Packages are better targeted with proportional funding, visible prices and modest co-payments.

This sends strong signals that direct effort, labour and taxpayer dollars to the people and services that generate the most value.

The reforms also go some way to easing intergenerational inequities. Because some costs are now means-tested against income, assets and growing super balances, older Australians who can afford it shoulder more of their own expenses; those without means still receive the full safety-net.

That reduces the subsidy the next generation would otherwise carry, easing inter-generational inequity while keeping universal, high-quality care within reach of everyone.

Fiscal outlook

Budgets are about priorities. The need for additional insurance against global risks will necessarily require careful prioritisation, and maybe reprioritisation, of areas of expenditure that are growing.

Next year, for the first time, expenditure on the NDIS is expected to exceed expenditure on defence. And in a world of increased uncertainty, we want a budget that maintains flexibility to implement policy responses to mitigate the effects on our people of possible negative outcomes.

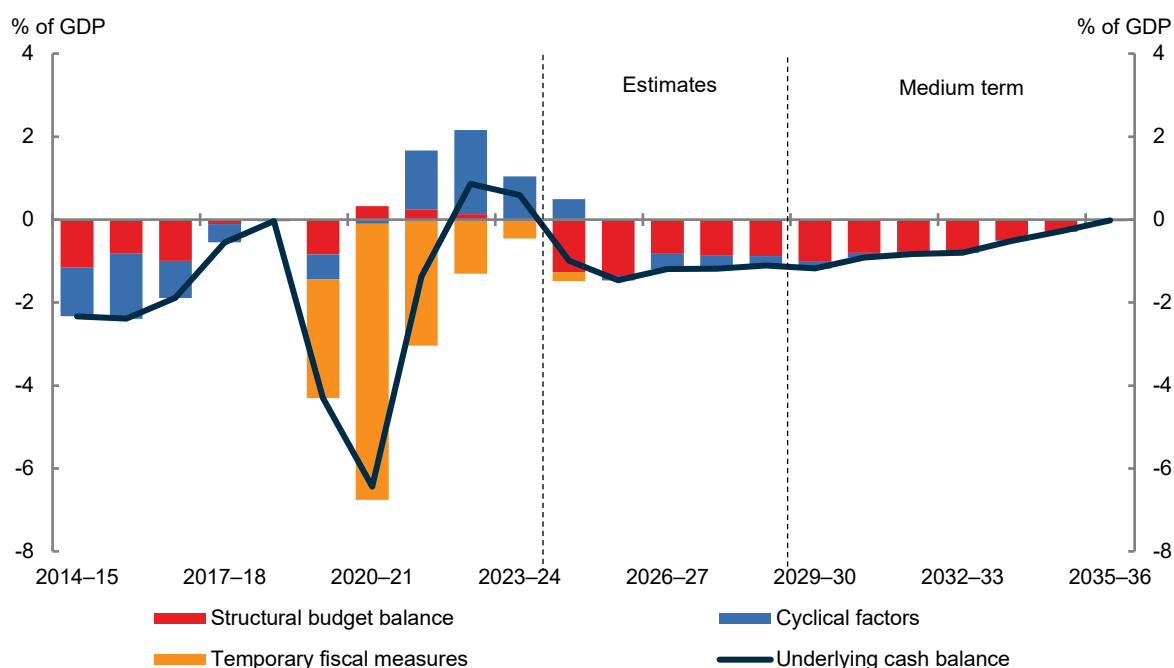
During its first term, the Government achieved two consecutive budget surpluses while delivering on a range of policy priorities.

Surpluses were achieved by returning a substantial majority of revenue upgrades.

All three major ratings agencies continue to rate the Government's debt at AAA, which is a valuable asset when financial markets are volatile. And minimises the borrowing costs that we have to pay.

But some of the strength in the budget position, for example from a high terms of trade, is temporary. This can be seen in the strong cyclical factors reported in the Budget. The structural budget position, is in deficit, expected to be at around 1½ per cent of GDP in 2025–26 (see Chart 8).

Chart 8: Structural budget balance



Source: 2025-26 Budget

The states and territories are also contributing to a deterioration in the aggregate fiscal position of all Australian governments.

Combined state and territory government debt is 18.9 per cent of GDP for 2024–25, the highest level since states assumed sole responsibility for managing their debt in the early 1990s.

The aggregate state fiscal deficit of 1.8 per cent of GDP for 2024–25 is 1.5 percentage points higher than the pre-pandemic long-run average.

Conclusion

Australia has handled the post-pandemic and war-generated inflation shock well. Inflation is within the target band and easing, growth is beginning to gradually strengthen, and unemployment remains at historic lows.

One of the areas the Government has invested in over the past 3 years is the social compact including addressing pay inequities in feminised industries and health and education outcomes. It has also eased cost of living pressures.

In the period ahead the policy focus shifts to responding to the Government's five policy pillars with the primary focus being on productivity and resilience.

The PC's upcoming report will undoubtedly provide the Government with valuable opportunities to pursue these challenges

However, there is already a substantial set of policies in front of government now that are material and will need to be delivered. The quality of decision making in responding to these reviews and policy challenges will be crucial to driving productivity.

This will need to be done while international risks remain high.

International economic and political fragmentation is accelerating, rules and norms are being cast aside, the interplay of nation size and power will dominate in the decades ahead.

This is not a new trend, it is an existing trend that has dramatically accelerated.

Nor is it a new world. We have seen this world before. It is one where missteps are more likely, and consequences more severe. A riskier and less predictable world.

But we can mitigate these risks through investing in our democratic capitalist economy.

This is the model of economic and social progress that Australian governments have championed in the past and is as relevant today as it was then.

It does need to be adapted to new challenges, such as the interplay of economic and national security, but it also needs to maintain the conventional economic considerations of budget constraints, trade-offs and cost benefit analysis.¹⁹

¹⁹ See Furman (2024), *Richard Cooper Lecture: In Defense of the Dismal Science*, <https://www.piie.com/sites/default/files/2024-09/furman2024-09-27.pdf>