Weekly economics podcast: The good news

By Perpetual Corporate Trust
8 December 2025

The good news is that the Australian economy grew in real terms by 0.4% q-o-q in Q3 taking annual GDP growth up from 2.0% y-o-y in Q2 to 2.1% y-o-y, one of the better economic growth rates in the OECD. Continuing the good news theme there is no recession in sight for Australia, something worrying forecasters at the beginning of 2025 and growth is sufficient to keep the unemployment rate low, around the 4.3% rate recorded in October, for many months to come. The good economic growth news, however, comes with a sting in the tail. Economic growth is threatening the speed limit imposed by low productivity for the Australian economy and that means inflation could stay higher than the RBA would like and force a return to rate hikes in 2026.

Returning to the Q3 GDP growth rate, the 0.4% q-o-q increase was driven by an over-sized 1.1 percentage point contribution from domestic demand. What prevented that big contribution from domestic demand showing fully in GDP growth were detractions to growth from a rundown in inventories, -0.5 percentage point contribution to GDP, and a -0.1-percentage point contribution from international trade (exports minus imports).

The very strong growth in domestic demand in Q3 was driven by household consumption spending, a 0.3 percentage point contribution (it was up 0.5% q-o-q, 2.5% y-o-y in real terms); a 0.2 percentage point contribution from government consumption spending (up 0.8% q-o-q, 2.6% y-o-y); and a 0.7 percentage point contribution from gross fixed capital expenditure, or investment spending.

Within gross fixed capital expenditure, housing investment contributed 0.1 percentage point to GDP in Q3 and was up 1.8% q-o-q, 6.5% y-o-y while real estate transfer costs – the costs associated with selling and purchase of existing homes – also contributed 0.1 percentage point and was up 5.0% q-o-q, 5.9% y-o-y. Very strong growth in spending on housing, evident in these Q3 numbers, is running up against very constrained supply partly because of especially poor productivity in home building and the construction sector in general. This is a worsening inflation flash point.

Something that may help to limit inflation over time, however, is the lift in productive investment spending in Q3. Investment in machinery and equipment contributed 0.3 percentage points to Q3 GDP and was up 7.6% q-o-q and 5.9% y-o-y. The lift in investment spending came predominantly from increased spending on data centres. This spending will over time facilitate greater use of artificial intelligence applications which may improve productivity.

Returning to productivity change (GDP per hour worked) in Q3, it lifted, but only by 0.2% q-o-q and 0.8% y-o-y. Productivity needs to rise at a much faster pace to prevent strong growth in domestic demand (+1.1% q-o-q in real terms in Q3) and wages (+0.8% q-o-q, 3.4% y-o-y according to the wage price index, but 1.7% q-o-q, 7.1% y-o-y in the Q3 compensation of employees contained in the National Accounts).

There is evidence that one key part of domestic demand, household spending, is growing faster early in Q4 than it did in Q3. Household spending in October rose in nominal terms by 1.3% m-o-m, lifting annual growth to 5.6% y-o-y, the fastest growth in more than two years and up from 5.1% y-o-y in September. Anecdotal reports of the ‘Black Friday’ sales in November point to more frenetic growth in spending in November.

While Australian households remain concerned about the cost-of-living, the sector has also had the biggest increase in disposable income over the past year in more than a decade. Household wealth has risen strongly too boosted by strong growth in house prices and financial investments. It should not surprise that household spending is lifting at rapid pace.

Strong growth in domestic demand in Q3 looks baked in for Q4 as well. That implies continuing upward pressure on inflation beyond the temporary factors that have taken the annual inflation rate above 3%. The Australian economy needs a tap on the policy brakes to bring growth back within the speed limit. That tap on the brakes could come from substantial and immediate cuts to government spending, a prospect that seems unlikely. Instead, the RBA will need to do the policy heavy-lifting.

Given recent data reports relating to domestic spending in Q3, household spending in October and higher-than-expected inflation reports in Q3 and in October, the RBA should be considering a rate hike at the policy meeting this week. Most likely, it will leave the cash rate on hold at

3.60%, preferring to wait for more data before hiking the cash rate. Our view is that evidence of strong domestic demand and high inflation will continue in the reports released before the first RBA policy meeting of 2026 in February. That meeting is live for a 25bps rate hike to 3.85%.

It is good news that the economy is growing strongly. It would be better news if productivity was growing strongly too.