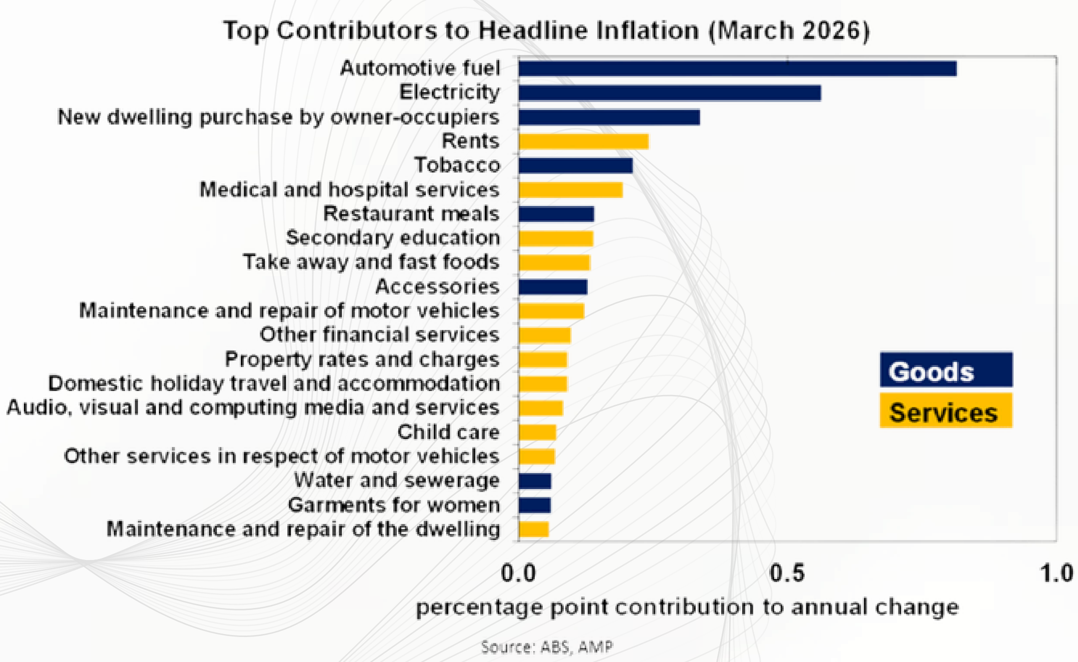
Weekly Economic Update

1 May 2026 | Inflation spike seals next week's RBA rate hike decision

This week's crucial inflation data landed with a softer thud than economists had feared. Inflation spiked to 4.6% in the year to March, a two-year high, from an annual rate of 3.7% in February. That's bad, but it wasn't as gruesome as economists had forecast. Still, the upside surprise on inflation relative to the RBA's pre-Iran forecasts means another rate hike next Tuesday pretty much is a done deal (see below).

The main driver of inflation last month was fuel prices, as expected, which bounced 33%. There was little sign of broader pressures (yet), but there were material price gains for electricity, home construction and rents (see chart below from AMP). Core inflation was steady at 3.3%, but still above target. The bad news is that the broader war-related price pressures are still to come, including for food, plastics, packaging, airfares and transported goods.

In terms of what it means for the Reserve Bank, recall that the last interest rate decision in March was narrowly split 5-4 in favour of a hike. But it's safe to say the "disagreement" among board members back then was about timing, not the direction of travel. For what it's worth, futures markets price around an 75% probability of a quarter point hike next Tuesday. That seems about right.



On fiscal policy, there's been more strategic leaks about likely measures in the upcoming Budget, which drops on 12 May. It now seems even more likely the government will dump the long-standing 50% capital gains tax discount in favour of the old, Keating-era inflation adjustment. This means a thinner discount (that is, a tax hike) and more complexity. The simple 50% discount was adopted in 1999 to avoid this.

There also are noises about limits being imposed on negative gearing. Existing investments will be grandfathered (so, no change for those), but it seems that only deductions for newly built housing will be allowed after May 12, if the whispers are to be believed. This will be a broken election promise if it comes to pass – the change to the CGT treatment is not.

More broadly, Treasury is awash with unexpected riches because of the war in Iran - it lifted energy prices, profits and tax revenue. The budget also will be helped by the NDIS savings announced last week, although higher inflation means sharper indexation of welfare payments. And this government cannot help itself – the budget will offer more untargeted cost of living relief. So, we'll still be staring at deficits for a decade and $1 trillion in public debt. You read that right.

Overseas, there were influential central bank meetings this week and the end-result was … nothing. The respective boards of the US Fed, the Bank of Canada, the Bank of Japan, the Bank of England and the European Central Bank all left interest rates steady. This leaves our own Reserve Bank way out in front as the early hiker. This gap on other central banks will widen next week.

The ebb and flow of negotiations about ending the war in Iran had an impact on financial markets. Crude oil prices surged when the US rejected Tehran's latest peace offering, but many equity markets recently were at record highs. Seems many investors are betting the war will end soon. The AUD touched a four-year high before receding.

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