

Weekly Economic Update



OPTIMAL
ECONOMICS

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Australia's economic chickens are coming home to roost because of a toxic mix of misguided policy decisions, ideology, neglect and laziness over many years. Just this week, both productivity and our living standards fell again, the cost of employing staff skyrocketed, house price falls accelerated, and we suffered our first trade deficit in years. That's quite a combo. Oh, and the government jammed its anti-aspiration tax increases through Parliament and there's a seemingly-endless war on.

Let's start with Wednesday's National Accounts. Australia's economy eked-out modest growth of just 0.3% in real terms in the March quarter, a sharp slowdown from the pace of growth at the end of last year. Annual growth in the economy remained at 2.5% only because of favourable upgrades. The slowdown largely reflects the RBA's rate hikes, weak consumer confidence and the initial impact of the war in Iran. Growth last quarter was propped up by the growing data-centre investment boom.

Most of the fall-out from the war - for growth and inflation - is still to come. So much so that there is a rising probability the economy contracts in the current quarter. The Reserve Bank has kept raising interest rates and confidence cratered to recession-like lows after petrol prices spiked. Moreover, the spike in diesel prices will cruel energy-hungry activity and many people cancelled holidays once travel costs spiked.

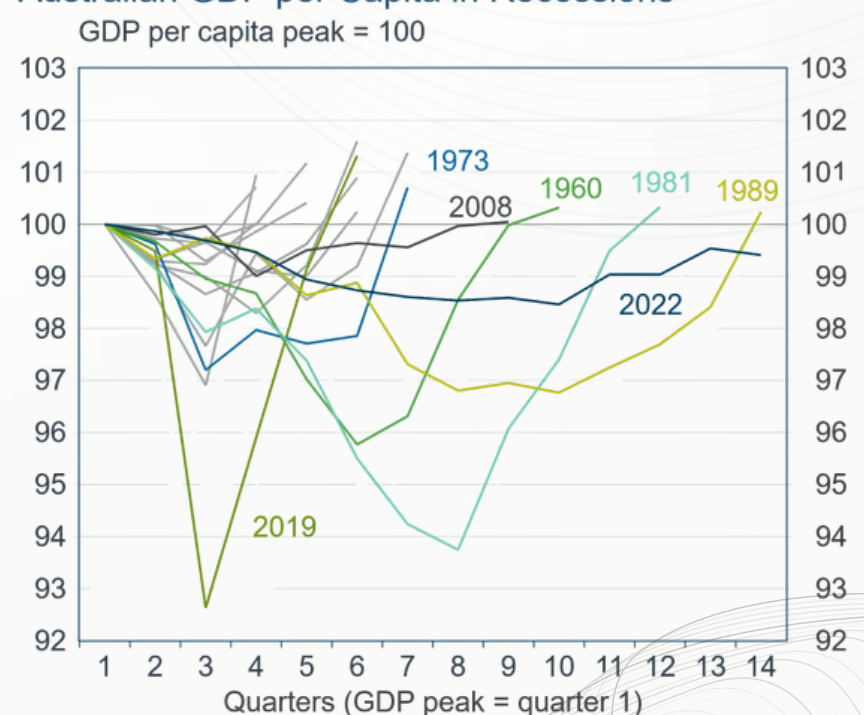
Will we suffer our first recession since the pandemic? Maybe, but the definition of a technical definition (back-to-back declines in real GDP) is past its use-by date. We didn't suffer a technical recession during the catastrophic global financial crisis of 2008-09. But the economic adjustment back then was brutal. This adjustment probably will be more modest, but the risks are rising.

As evidence, living standards continue to be crushed by our terrible productivity performance. Per capita GDP fell for the 10th time in the last 15 quarters in Q1, an unprecedented run of failure (thanks to Jonathan Kearns at Challenger for the brilliant chart below). This extended per capita recession is partly because productivity growth was negative again last quarter, after no growth at all in Q4 last year - productivity now is lower than it was back in 2019.

Also revealed this week was the dismal news that house prices in Sydney and Melbourne fell in May, with the rate of decline accelerating. It's tempting to blame the recent budget that targeted aspiration and wealth accumulation, but the RBA's rate hike in early May also was unhelpful. Auction clearance rates last weekend tumbled to a six-year low at a level consistent with even larger falls in house prices.

Meanwhile, the Fair Work Commission announced that Australia's minimum wage will rise by an above-inflation 4.75% from 1 July and that lowest paid workers will receive an even juicier 6% gain. (*continues over the page...*)

Australian GDP per Capita in Recessions



Note: year denotes the pre-recession peak of GDP; the grey line recessions are 1965, 1970, 1971, 1975, 1977, 1985, 1987 and 2000
Sources: Challenger, Macrobond, ABS

How businesses will pay for that without substantial price hikes, productivity offsets or job cuts is anyone's guess. Remember, only people still with a job at the start of July will receive the wage increase.

All the while, the Government is making an even bigger mess of selling its contentious budget. Polling suggests the proposals were toxic to most demographics, including those said to benefit, so good luck with the sales job. The government rammed its budget measures through the lower house of Parliament this week, but also says it is contemplating carve outs from the capital gains tax hikes. Stay tuned for news on those.

Finally, Australia's population this week ticked up over 28 million people. Increasingly, our population grows via net inwards migration because the birth rate is plunging, as in most developed countries. The official population clock says one person arrives to live in Australia every 59 seconds and that an Australian leaves to live overseas every 2 minutes 35 seconds. You do the maths.



Stephen Walters
Chief Economist,
Optimal Economics

Call us:

+61 499 976 196

Email:

stephenwalters@optimaleconomics.com.au

Website:

<https://optimaleconomics.com.au/>