OPTIMAL ECONOMICS

Weekly Economic Update

Budget measures clearly contributing to the weakness in the housing market

The federal government maintains the folly that its contentious tax changes aren't contributing to the obvious softening of the national housing market. This is despite all evidence to the contrary. Official spokespeople still doggedly stick to the Treasury line that house prices will "continue to rise", albeit by slightly less than before.

Except, house prices aren't rising. Out in the real world, national home prices this week fell at their fastest rate in four years, with the falls in the dominant Sydney and Melbourne markets accelerating. Further house price falls are coming, too, given the traditionally tight relationship between home prices and auction clearance rates, which have cratered since the budget.

A poll out this week showed that many people welcome lower house prices on the assumption it improves affordability. But most of those for whom a house is their biggest asset will not. On housing affordability, it's not clear how the budget measures will add to housing supply, which continues to fall well short of demand. This is particularly so with surveys this week showing construction industry sentiment collapsing since the budget.

The budget measures are not solely to blame, but they're definitely playing a role. Even the Reserve Bank indicated as much this week in the minutes from the latest Board meeting. Home prices in Sydney have been falling for seven months now, so other factors clearly are at work. For sure, the RBA's three interest rate hikes earlier this year have helped cool house prices, as has falling sentiment about the economy and soaring energy costs, including for petrol.

And there could be more interest rate hikes from here. The minutes from the RBA board meeting confirmed the Bank retains a "tightening bias". That is, interest rates are more likely to rise from here than fall, and futures markets still price a decent chance of further rate hikes. This reality could be spooking some potential homebuyers.

We know that investors hate uncertainty, though, and the government is building the plane as its flying it. That became clear last week during the unseemly scramble to get the tax measures passed through Parliament, alongside government pledges to scrape remaining barnacles off the legislation, including the so-called "widow's tax". No wonder rattled investors are fleeing.

The end of the financial year this week triggered a bunch of changes. Most of us received a modest income tax cut (announced back in the 2025 budget), the big rise in the minimum wage kicked in, paid parental leave was extended, pay-day super started, and the higher tax on large super balances began.

Also, businesses now can carry back losses and the immediate write off of $20,000 for asset purchases became permanent. These are among the few measures in the budget that might help lift our dismal productivity growth. Might.

The bad news? The government is pumping even more money into an already capacity-constrained economy. This means some of the changes inevitably will add to inflation, which already is way above the RBA's target. The big pay boost for the lowest income earners, who typically spend all their wages, is not pegged to improvements in

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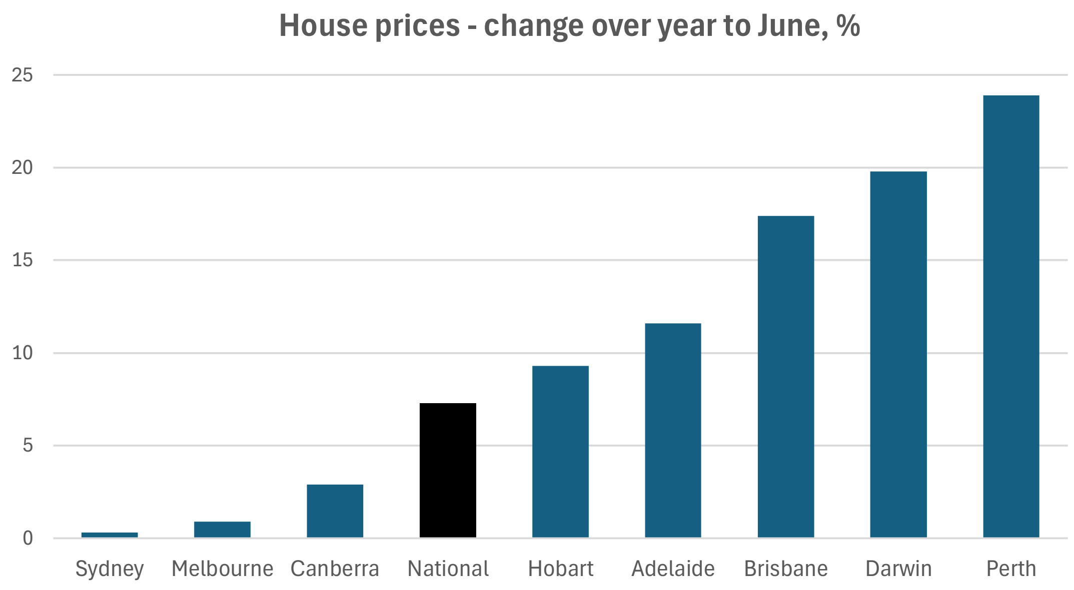
productivity which, we all know now, is the lowest in six decades! This will end in tears.

In markets, it was a tough financial year. The US equity market soared 20% over 2025-26, but the local ASX failed to beat bank interest. This is despite a 50% gain for the Aussie miners. Gold has sagged 30% over the last few months, albeit from record highs, and oil prices now are back to where they were when the war with Iran started back at the end of February. It certainly was a wild ride but, as with all rollercoasters, we finished back where we started.



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