iPartners inFocus
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Budget 2026: never waste a good crisis!

- The Budget deficit is put at $31.5bn (1% of GDP) in 2026/27, an improvement on earlier estimates.
- Deficits run around the 1% of GDP mark thereafter before slowly declining to balance by 2034/35.
- Gross debt, as a share of the economy, peaks at 35.8% of GDP in 2028/29.
- The pace of fiscal repair remains painfully slow.
- Budget forecasts show a sluggish economy and rising unemployment. But not a recession. Or stagflation.
- Measures were more reform focussed than seemed likely a few months ago. With some political risk.
- Fiscal policy is unlikely to prevent the RBA lifting interest rates again.
- The appetite for intergenerational equity looks overdone and may have some unintended consequences.

There is an old adage about "never wasting a good crisis". The government appears to have taken this to heart. We have ended up with a set of fiscal measures that were more reform focussed than seemed likely a few short months ago. And one where the government was willing to bear more political risk than timid politicians typically want to hold.

From that perspective, the main "surprise" was the depth of productivity measures implemented. And the $13bn boost now expected to long-run GDP.

The main "disappointments" relate to the decision to put changing tax arrangements for oil and gas companies into the too-hard basket, despite current windfall profits.

The net effect of policy bravery is an improvement in budget bottom lines. But fiscal repair remains painfully slow. To top it off, the ever shifting global backdrop means that the amount of "rubber" and increase in "guestimation" mean this year's Budget figuring should be treated with great caution.

Treasury boffins would have had a torrid time in framing the 2026 Budget. The global backdrop is shifting on an almost daily basis. Geopolitics, the Iran War and oil moved to central focus. The *domestic* Budget objectives have evolved as a result.

The relatively benign backdrop in H1 2025 (and a May Election) allowed a focus on ALP priorities like tax cuts for the lower paid, Medicare, pharmaceutical benefits and childcare. Fiscal repair was a low priority.

Figure 1

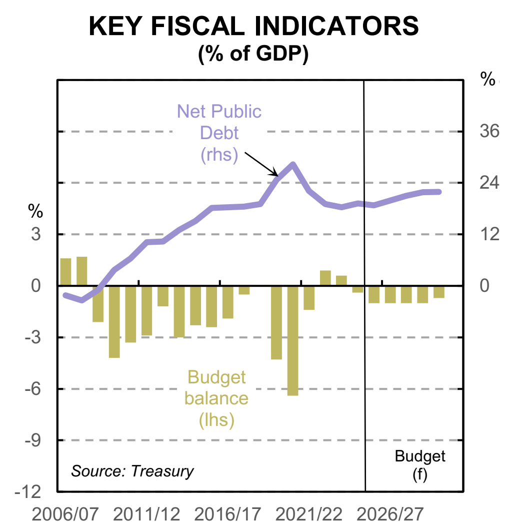
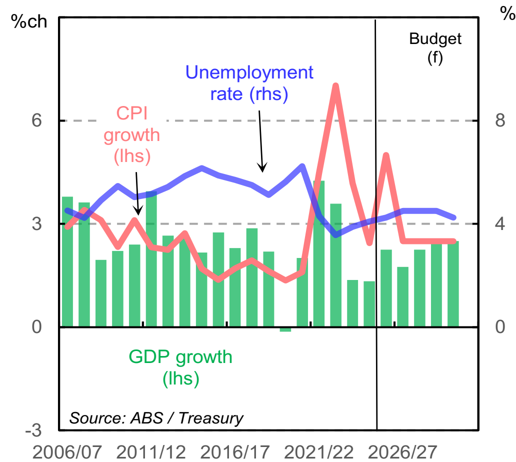


Figure 2



The inflation debate in H2 2025 and whether the government was helping or hindering the RBA in pursuit of its inflation target meant a shift in focus to "savings" and Budget repair.

But an oil price spike and supply chain disruption in March 2026 courtesy of the Iran War meant a refocus to cost-of-living relief and promoting economic resilience. A productivity focus and something called "intergenerational equity" are to provide the smokescreen to cover the difficulty of satisfying everyone at the same time (including the RBA in their fight against inflation).

A quick game of Budget Bingo reveals the importance of these themes. Words like "savings", "resilience" and "fairness" were on high rotation in the Treasurer's Budget Speech.

Figure 3

Just the numbers

The consistent message from Canberra in the run up to the Budget was the difficulty of balancing relief, restraint and reform in uncertain times.

The initial read of the Budget numbers suggests policy makers have had some success in dealing with these conflicting objectives. The underlying budget deficit tracks sideways during the standard four-year forecast period (Table 1). Those deficits are on a *declining* track as a share of GDP and are *smaller* than the last official forecasts in the December 2025 Mid Year Economic & Fiscal Outlook (or MYEFO for Budget afficionados).

Deficits persist in the projection period out to 2033/34. But budget balance is achieved in 2034/35

and surpluses then emerge. Those balances are also improved on earlier estimates that remained in deficit as far as the eye could see.

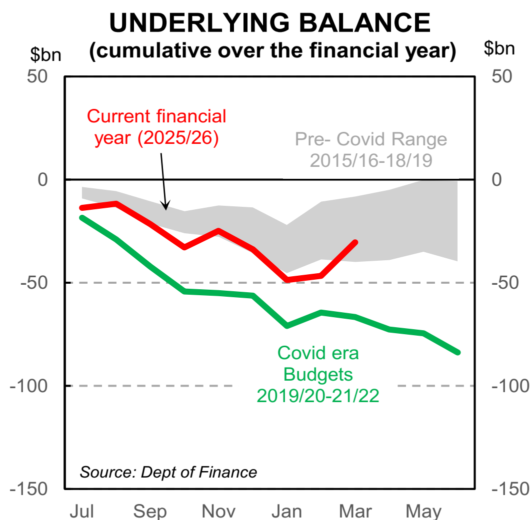
Table 1: Key Budget Aggregates ($bn)

	25/ 26	26/ 27	27/ 28	28/ 29	29/ 30
Revenue	760	798	823	848	895
Payments	788	830	854	883	920
Underlying Balance	**-28.3**	**-31.5**	**-31.0**	**-34.4**	**-25.3**
(% of GDP)	*(-1.0)*	*(-1.0)*	*(-1.0)*	*(-1.0)*	*(-0.7)*
Off-Budget spending	-20	-33	-23	-23	-16
Headline Balance	-48	-64	-54	-57	-41
Net Debt	**556**	**617**	**669**	**726**	**768**
(% of GDP)	*(18.8)*	*(19.9)*	*(21.0)*	*(21.8)*	*(21.9)*

But there are some concerning trends below the surface.

Firstly, the budget deficit for the current financial year (2025/2026) is now put at $28bn (1.0% of GDP). An improvement on earlier estimates for sure. But the trajectory *through* the current year (Fig. 4) is running at or below the "normal" (pre-COVID) range.

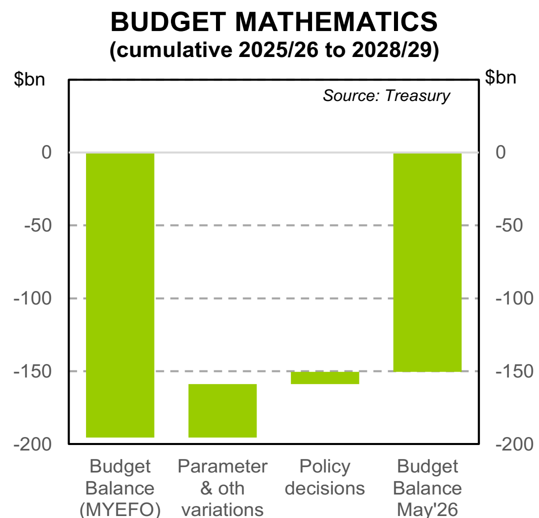
Figure 4



Secondly, the government has delivered on its promise to "bank" temporary revenue gains. But the overall improvement over the next four years reflects an odd $19bn spike from policy changes in 2029/30. This spike comes as NDIS savings and tax changes kick in.

The expectation in the December 2025 MYEFO was that the Budget balance would cumulate up to a deficit of $195bn over the five years to 2029/30. The Budget mathematics (Fig. 5) now show that parameter & other variations - or "the economy" - will improve the budget bottom line by $37bn over the period. And, as noted, a last-minute spike from policy initiatives in 2029/30 contribute a further $8bn improvement.

Figure 5



The cumulative budget deficit over the next five years now stands at $150.5bn.

Thirdly, there is now a question of which budget measure should we focus? We are spoilt for choice. We have:

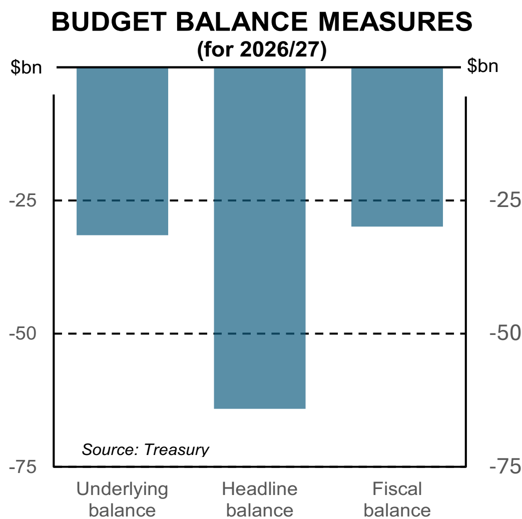
- the *underlying* balance (the current preferred measure);
- the *headline* balance (the traditional focus); and
- the *fiscal balance* (something for policy wonks only).

The figures for 2026/27 show deficits ranging between $30bn and $60bn (Fig. 6).

Back in the 1980s and 1990s the main job for economists on Budget night was to work out the "true" picture. The *headline* figures were flattered by the proceeds of the privatisations of the time. Treasurer Costello helped us out by publishing the *underlying* balance that excluded privatisations.

Good for economists but not so helpful for politicians more concerned with the Budget optics. The "solution" was to shift increasing amounts of spending Off Budget.

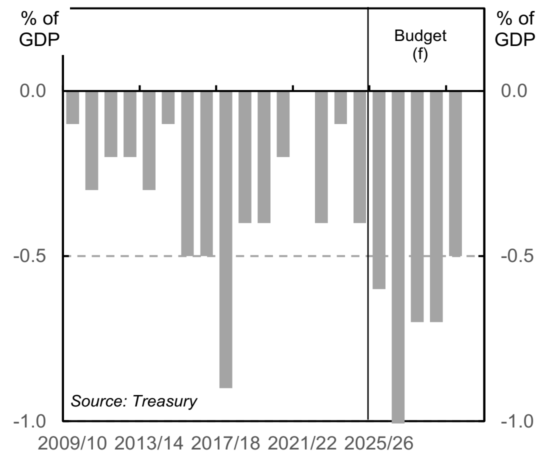
Figure 6



Off Budget is where the Government parks spending on projects that should ultimately prove self-funding and so can be repaid. Examples include the NBN, student loans, Housing Australia and Snowy Hydro.

Treasurers of all persuasions have used this facility since the NBN was first proposed. And Budget 2026 is no exception. Proposed off-budget spending amounts to $114bn over the period to 2029/30, averaging out at around 0.7% of GDP per year (Table 1 and Fig. 7).

Figure 7



For the non-policy-wonks, the fiscal balance is an *accrual* measure (rather than a *cash* measure). It focuses on when revenues are earned and expenses incurred.

Bottom line: there is a strong case to shift focus back to the headline balance in Budget analysis.

Headline Budget deficits persist during the Budget forecast period and accumulate up to $265bn by 2029/30. This outcome is a much less impressive performance than suggested by the underlying balance.

Finally, the headline balance is also the better indicator of government financing requirements and the resultant pressure on financial markets (Table 1).

The inescapable result of ongoing headline deficits is that Commonwealth government debt will continue to rise.

Gross debt is set to finally surpass the $1 trillion mark. This politically sensitive level was first forecast by the Morrison government in 2022. The then Opposition used that forecast at every opportunity to beat up the government. (It didn't happen). The LNP returned the favour when the ALP took over the fiscal reins. (Still hasn't happen). But it looks like we will get there in 2026/27.

That said, the projections show the peak in gross debt, as a share of the economy, is now sooner (2028/29) and lower (35.8 % of GDP).

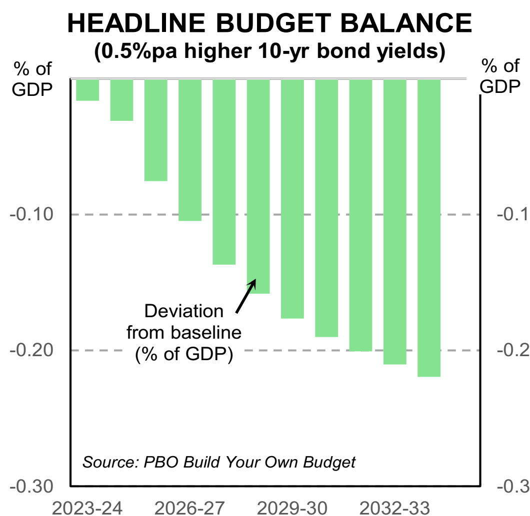
Net interest payments on government debt rise from 0.6% of GDP in the current financial year to 0.9% by 2029/30. Interest payments are the fastest growing component of government spending over the medium term.

Net interest payments are now a large enough share of government spending that changes in borrowing costs can affect the size of the deficit.

The Budget figuring assumes that the weighted average borrowing cost will be 4.8% (up from 4.4% in the MYEFO estimates).

The *Build Your Own Budget* simulator developed by the Parliamentary Budget Office (PBO) allows some sensitivity analysis. Adding a ½% to bond yield assumptions, all else unchanged, would push prospective headline Budget deficits up by 0.1-0.2% of GDP over time (Fig 8).

Figure 8



More broadly, the Budget is predicated on real GDP growth of only 1¾% in 2026/27. And growth remains sub-trend until 2028/29. It is a weak growth profile that means per capita GDP will fall further. And real wages will decline.

Sluggish employment growth is one outcome. So is a continuation of our dismal productivity performance. Rising unemployment is another.

But how bad is it? It's not a recession. It's not stagflation. Jobs growth remains positive. And an unemployment rate peaking at 4½% is not too far off fifty-year lows.

Budget economic forecasts are summarised in Table 2.

Table 2: Key Forecasts (%pa)

	25/26	26/27	27/28
Real GDP	**2¼**	**1¾**	**2¼**
Employment	1½	1½	1¾
Unemployment (%)	**4¼**	**4½**	**4½**
CPI (yr to June)	5	2½	2½
Wages (yr to June)	3¼	3½	3½
Terms-of-trade	4½	-¼	-7¼
Nominal GDP	**6¾**	**4¼**	**2¾**
Current account (% of GDP)	-1¾	-2¾	-4

Source: Treasury

The main forecasting "surprise" is the speed of the return in inflation rates to the RBA's 2-3% target range. The Budget states that "inflation is forecast to sustainably return to the RBA's target band in the middle of 2027". This is an extraordinary outcome relative to the rhetoric elsewhere in the Budget papers that talks about the upside pressures. It's also an extraordinary outcome relative to the RBA's own forecasts for underlying inflation that don't reach the target midpoint until mid 2028.

Referring again to the *PBO's Build Your Own Budget simulator* allows some inflation related sensitivity analysis. Adding a ½% to CPI assumptions, all else unchanged, would reduce headline Budget deficits by 0.1-0.2% of GDP over time. Government revenues are more leveraged to inflation than spending.

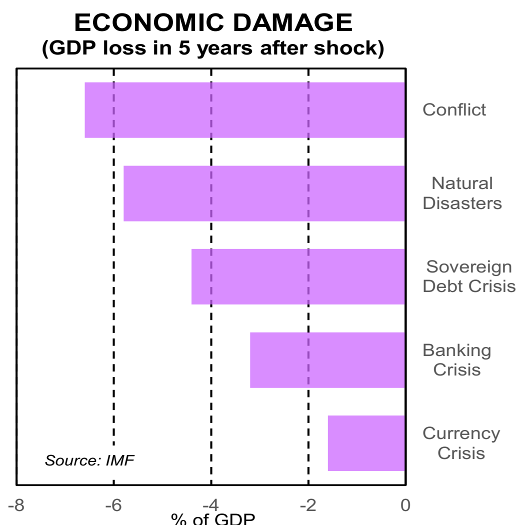
Eventual falls in commodity prices mean a falling terms-of-trade and the emergence of quite large current account deficits. This set of assumptions mean that Australia is losing the "protection" in

global funding markets provided by a current account surplus. That protection would have been quite useful in the current global environment.

Everyone will agree that Budget estimates are "rubbery". And economic projections are really just "informed guesses". But the amount of rubber and increase in guestimation mean this year's Budget figuring should be treated with great caution.

This warning is particularly appropriate given IMF research that looks at the shocks that hit the global

Figure 9



economy from time to time. Their conclusion: "conflict" causes the most economic damage (Fig. 9).

IMF estimates put the cost of "conflict" as approaching 7% of GDP over a 5-year period. That far exceeds the damage associated with financial crises and severe natural disasters.

More broadly, economic projections these days cannot be presented without being accompanied by alternative (worse) scenarios for key Budget drivers. And it's fair to say that scenario analysis is entirely appropriate in the current uncertain environment.

Treasury scenario analysis looks at what happens if oil prices peak at USD200 in Q3 2026. Prices then subside back to USD80 by Q2 2029. The implications are pretty ugly:

- the *level* of real GDP is ½% lower in 2026/27;
- Inflation peaks at 7¼% at the end of 2026; and
- unemployment peaks at around 5% in 2027/28.

Judging the Budget

Treasurer Chalmers has given us a roadmap on how he would like Budget initiatives to be judged. The key markers are:

- Is it fiscally responsible?
- Does it help with the cost-of-living squeeze (without making the inflation outlook worse)?
- Does it improve living standards?
- Are Budget initiatives "quality"?
- Does it improve productivity and resilience?
- Will it aid intergenerational equity?

So how should we score Budget 2026?

I. Fiscal responsibility

The first question on Budget night is always what is the bottom line? Surplus or deficit?

Treasurers of all persuasions have attempted to shift the focus from the Budget as an accounting ledger to the Budget as a medium-term strategy. So deficits are OK as long as they fall over time and fiscal sustainability is achieved.

This focus is actually quite reasonable. Nobody expects the RBA to achieve its 2½% CPI target each quarter. And most economist at least would approve RBA actions so long as they show inflation returning to target over a reasonable time frame.

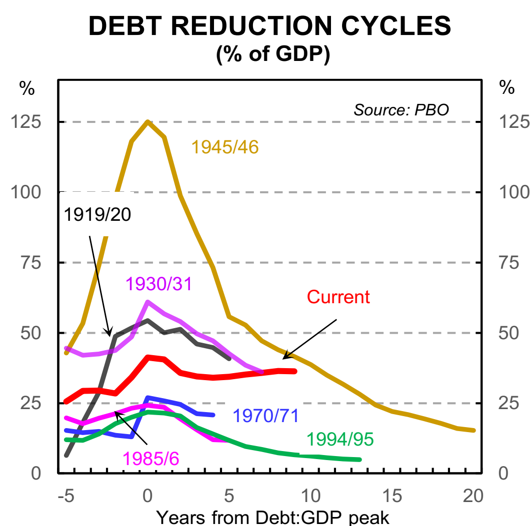
Budget 2026 does show a declining Budget deficit trajectory. But "balance" and "surplus" lies somewhere way over the horizon.

Longer term, deficits and debt grow at a slower pace than nominal GDP. This outcome means the deficit:GDP and debt:GDP ratios fall. The government seems happy to take this downward

trend as a sign that fiscal sustainability has been achieved.

But the reality is that the dismal fiscal repair performance of the past decade continues in this Budget (Fig. 10). The lack of debt reduction is clearly disappointing when benchmarked against previous consolidation cycles.

Figure 10



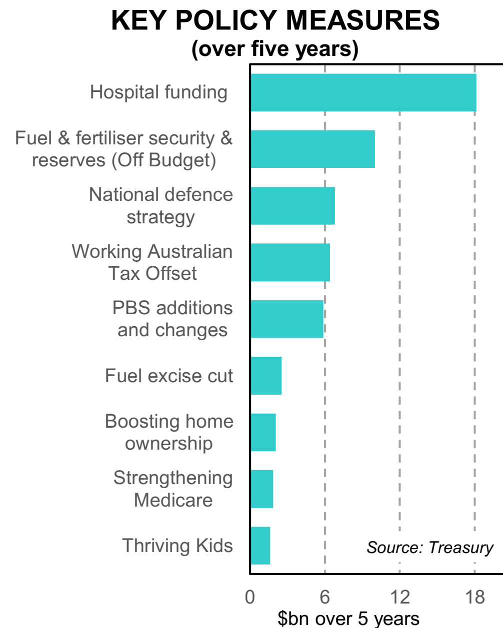
Governments with a stonking majority in the first year of their term quite often make "brave" decisions. And pruning the NDIS and the changes to capital gains tax , trust taxation and negative gearing are bold. Certainly these policy changes were seen as too bold and were junked in the run up to the 2025 Election.

Fiscal responsibility is also predicated on "banking" any benefits delivered by the economy (such the revenue from higher energy prices). And on prioritising savings over spending.

The government deserves credit for delivering on these fronts (Fig. 11). Nevertheless, the temptation to "hide" some measures off-budget was too great. A large share of the fuel security package sits off-budget as financial assets and financing support.

Big ticket items include hospital funding as part of the National Health Reform Agreement, more defence spending, a new Working Australians Tax Offset, new listings for the Pharmaceutical Benefits Scheme (PBS) and the cut in fuel excise (Fig 11).

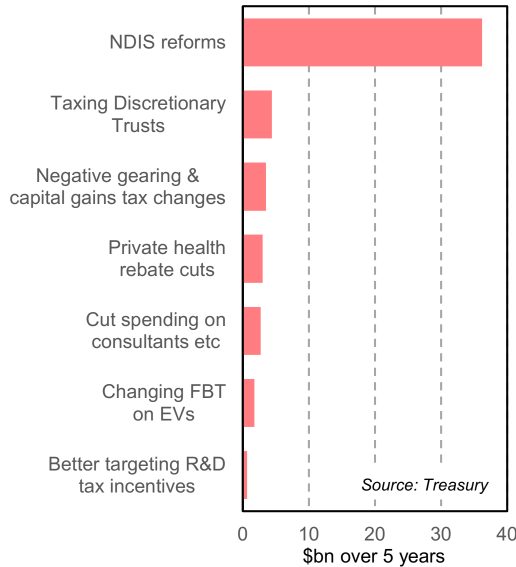
Figure 11



Savings measures centre on the proposed changes to the NDIS. Other significant contributors are the new taxes on trusts and the changes to negative gearing and capital gains taxes (Fig. 12).

Some of the savings measures are the old accounting trick of "reprioritising" spending. Cancelling the Inland Rail and diverting some of the savings to the Melbourne Rail Loop is an example. Old Budget hands will recognise this as the robbing Peter to pay Paul accounting trick. Other tired old favourites like strengthening tax compliance and getting rid of consultants are also in play.

Figure 12



Redefining is another useful accounting tool. Defence spending, for example, has been redefined to include pensions and veterans expenditures. This shift boosts apparent defence spending from around 2% of GDP to 2.8%. Or not far off the government's 3% target. It seems the accountants pen is indeed mightier than the sword! Hopefully President Trump will be pleased!

II. The cost-of-living, inflation and the RBA

The most important issue that households think governments should focus on is the cost-of-living (Fig. 13). Housing supply & affordability follow close behind.

When probed further, households nominate food, electricity, health costs, insurance, fuel and mortgage payments as the most stressful cost-of-living pressures.

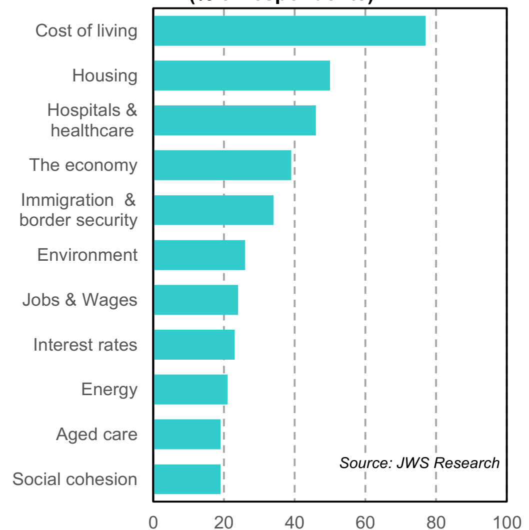
Household will probably be disappointed with the modest cost-of-living initiatives from that perspective.

The main measures are a $250 Working Australians Tax Offset (WATO no less), a $1,000 instant tax deduction, the temporary reduction in the fuel excise levy, and additional PBS spending to lower medicine prices.

What stands out about these measures is their temporary nature (fuel excise cuts) or delayed start (the WATO does not start until 2028/29).

The past approach in uncertain times was: Go Hard. Go Early. Go Households.

Figure 13



Policy makers have also been at great pains to remind households of earlier support measures. These include the two smallish tax cuts announced last year.

Nevertheless, the government deserves credit for keeping their nerve and limiting cost-of-living relief. And that some measures come with a sunset clause to prevent any longer lasting fiscal impact.

The government also deserve credit for skewing housing-related measures towards the supply side of the equation. Policies include a $2bn fund for housing infrastructure (roads, water, sewerage etc). The claim is that this fund will enable an increase in new housing supply of 65,000 dwellings.

The changes to negative gearing and capital gains tax are also being presented as favouring housing supply as well.

The general consensus among economists is that changing negative gearing and CGT may improve housing affordability. Particularly if the reforms are

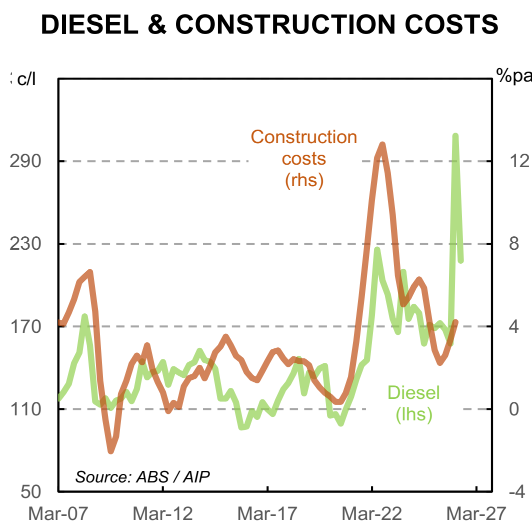
successful in steering investment toward building new homes.

Treasury modelling suggests that the reforms will lower the investor share of the housing market and increase the owner-occupier share of by around 75,000 dwellings.

The same modelling suggests that lower investor demand will slow (not reduce) dwelling price growth. Rents may actually *increase*.

Paradoxically, attempts to lift supply may prove inflationary. The measures come at a time when the spike in oil/diesel prices is set to sharply increase construction costs (Fig. 14). Surveys show that capacity use in the construction sector is already elevated. And the Civil Contractors Federation reports that higher diesel prices mean that 33% of their members are looking to pause construction activity. And 50% are considering cutting their workforce.

Figure 14



The government has also resisted new policy changes to help first-home buyers.

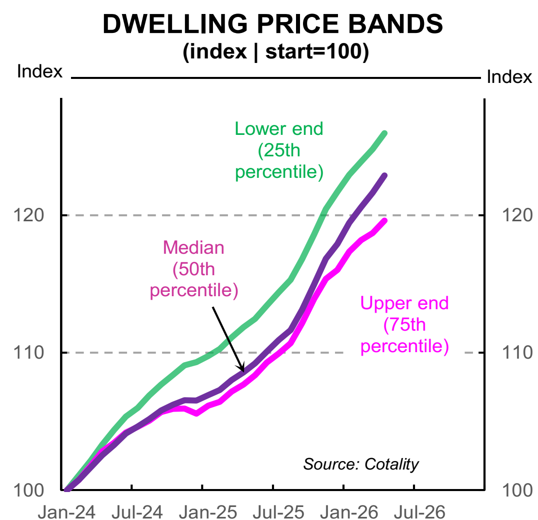
Any economist will tell you that incentives to first-home buyers boost demand and are rapidly built into dwelling prices.

Cotality, the property insight research company, notes that the government's 5% deposit scheme boosted competition for entry-level homes. And so increasing prices for first-home buyers over time.

Homes below first-home buyer price caps are rising faster than more expensive properties (Fig. 15).

The mortgage part of household stress will be determined by how the RBA sees the Budget. And what it means for the inflation outlook.

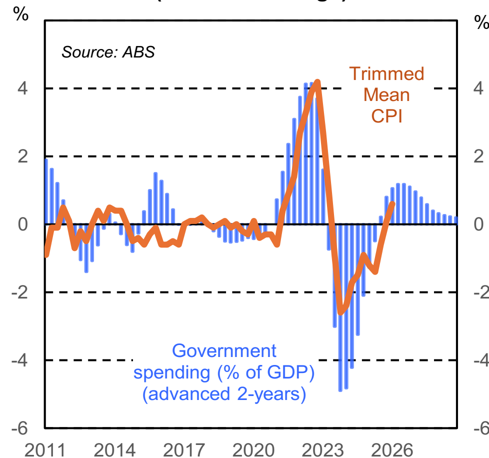
Figure 15



RBA-Government debates are typically carried out behind closed doors. But the demand-supply, or public vs private spending, disagreement has spilled out into the open.

The fundamental inflation issue from the RBA perspective is that demand is pushing up against supply. The government argues that *public* spending growth has slowed. And that inflation pressure is coming from rising *private* sector spending.

Figure 16



The budget shows public spending growth of 2¾% in 2026/27 and 2½% in 2027/28. That flat trajectory does not look like much of a slowing. And spending as a share of GDP remains at an elevated 27% of GDP. Swings in the share of government spending within the economy have proved a useful guide to the direction of inflation momentum (Fig. 16).

In the end its total demand that matters for the RBA. The source of that demand is irrelevant. Fiscal policy adds to the case for further RBA action.

After three 25bpt rate rises so far in 2026, the RBA now describes current policy settings as "a bit restrictive". A pause now seems likely with probably a further 25bpt lift at the August meeting. That would take the RBA cash rate to 4.6%.

The risk is that any housing supply benefit is offset by a deterioration in affordability.

The Budget was formulated against a background where stagflation risks are being debated. The last genuine period of stagflation was from 1973-83.

Budget forecasts look nothing like stagflation (Table 3).

Table 3: Stagflation

	Stagflation (1973-83)	Budget (f) (2026/27)
GDP deviation from normal (%pa)	-1.1	-½
Unemployment rate peak (%)	10.3	4½
Inflation rate peak (%pa)	17.5	5

Source: ABS / Treasury

Stagflation is difficult for central bankers. Especially those like the RBA that have a dual mandate of low inflation and full employment. But the RBA has made it very clear. It's an inflation-first strategy (as it was back in the 1970s/80s). The mantra then was the best contribution that the RBA could make to economic prosperity and full employment was to keep inflation rates low and stable.

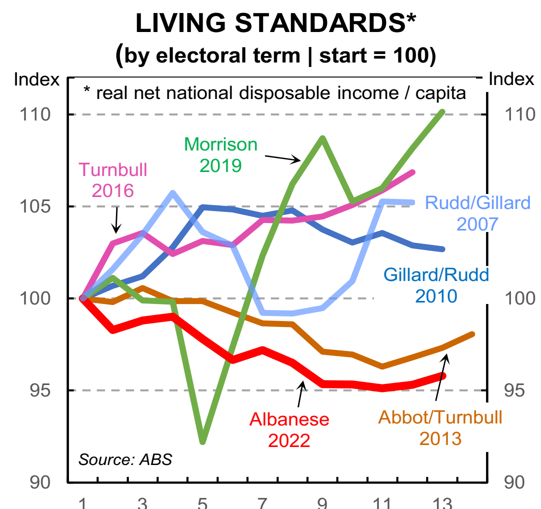
III. Living standards

The desire to improve living standards is the flip side of the observation that many people feel worse of than they were a year ago. Five years ago. And so on.

The evidence is there.

Economists will tell you the best measure of living standards is Real Net National Disposable Income per capita. RNDI per capita fell by around 5% over the past four years – the largest sustained decline by electoral term (Fig. 17).

Figure 17



RNDI is a bit of a mouthful. But what it means in simple terms is that living standards are a function of real wages and productivity less costs.

The key points from the Budget are:

- The forecasts show any real wages growth is unlikely before mid 2027.
- Productivity growth is negligible over the next two years. And will run behind population growth.
- Cost of living relief is small and temporary.

Some measures targeting living standards come with risk attached. The main concern is that improving household cashflow today may worsen inflation, housing affordability and fiscal sustainability tomorrow.

The government submission to the Fair Work Commission's Annual Wage Review, for example, argues for a "sustainable real wage increase". A large wage rise at a time of weak productivity growth could add to underlying pressures.

IV. "Quality" of Budget initiatives

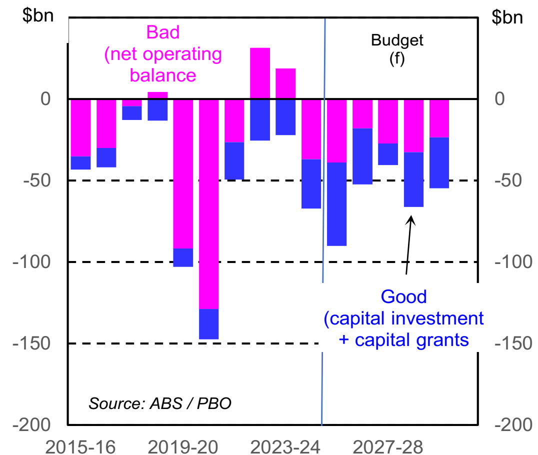
The Treasurer has long argued that Budgets should be judged not only on spending and debt - but by the *quality* of the policy initiatives. Or what do they do to they lift productivity, resilience and long-term growth?

The "quality" angle has some similarities to the debate started by the previous Morrison government on "good" debt vs "bad" debt.

- "Good debt" is borrowing to fund infrastructure and investment that boosts future economic growth and generates returns.
- "Bad debt" is borrowing to fund day-to-day government spending or recurrent expenditure.

Budget 2026 figuring shows that a fair amount of the borrowing requirement is to fund "good" debt (Fig. 18).

Figure 18



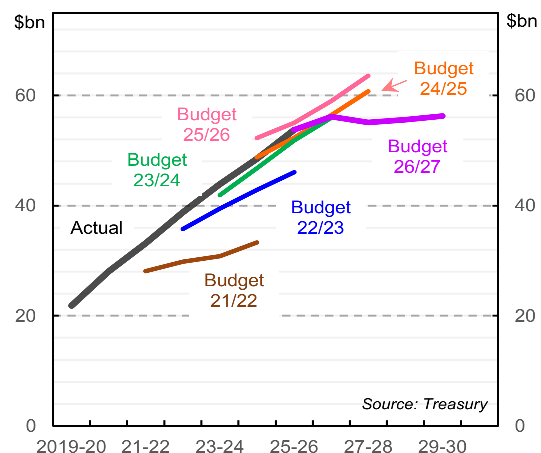
The same "quality" lens should also be applied to Budget savings initiatives.

Budget savings are dominated by changes to the NDIS. There is a long history of actual NDIS spending exceeding projections (Fig. 19).

The original NDIS design envisaged long-run growth of 5-6% per year. Actual growth had run at 10-18% per year over the past five years. The overrun reflects underestimation of the number of participants and the intensity of support required.

The aim is to reduce spending growth to 2% per year (versus the previous target of 8%). The expected savings over the next four years is put at $36bn.

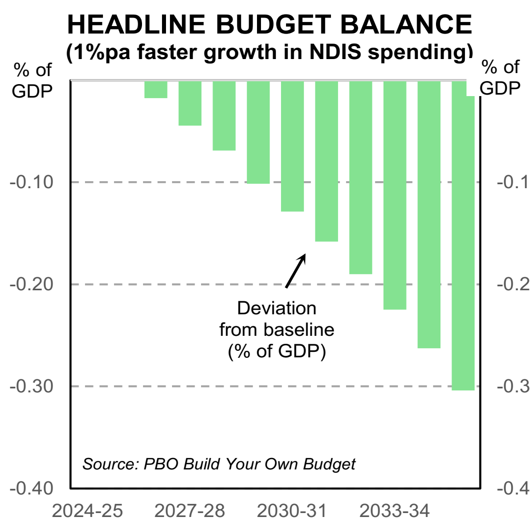
Figure 19



The savings rely on cutting the number of recipients and changing eligibility determination. How these changes will be achieved in practice is unclear. But it does seem that some spending is being pushed back on to the States. This does not seem a "quality" outcome.

The reliance on capping NDIS growth at 2% per year is potentially a major source of error in Budget projections.

Figure 20



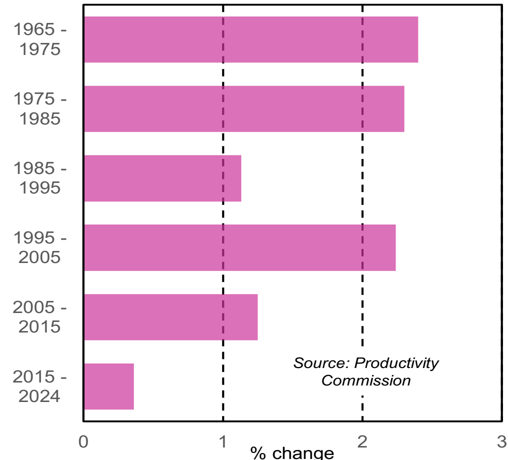
The *Build Your Own Budget* simulator developed by the PBO allows some sensitivity analysis. Adding 1% per year to NDIS growth, all else unchanged, would push prospective headline Budget deficits up by 0.3% of GDP over time (Fig 20).

V. Productivity & Resilience

The weakness in Australia's *productivity performance* is well known. Productivity growth is in negative territory (Fig. 21). And the decision by Treasury to downgrade its estimates of long-term productivity growth is particularly concerning. Productivity growth in budget figuring now assumes the return to trend is delayed to 2030/31!

This downgrade means slower income growth and harder budget repair unless productivity reforms succeed.

Figure 21



Small wonder that Budget rhetoric stresses many initiatives have a productivity focus!

The range of measures with a productivity tag highlights the importance that policy makers now put on the issue. Many of the initiatives have been taken from the productivity agenda developed by the Productivity Commission (Table 3).

The main initiatives include:

- Streamlining approvals and business regulation.
- A new $2bn Local Infrastructure Fund tied to state productivity reforms.
- The $20,000 instant asset write-off made permanent for small business.
- A streamlined pathways for skilled migrants to enter the workforce more quickly.
- Policies intended to increase business investment and R&D.
- Investment in digital infrastructure and AI capability.
- Changes to negative gearing and capital gains tax may help reallocate capital toward more productive investment.

Table 3: Productivity Commission Agenda

What should governments do?

Promote dynamism & resilience via investment

- Change corporate tax system to encourage capex (tax rate to 20% for small companies)
- Permanent instant asset write-offs
- Reduce red tape and regulatory complexity

Find lowest cost route to meet climate change

- Replace subsidies with market-based incentives (inc fuel tax credit for heavy vehicles and FBT exemption for EVs)
- Faster clean energy approvals
- Better transmission planning

Realise gains from the digital revolution

- Expand digital ID systems
- Encourage AI and automation adoption
- Improve data sharing frameworks
- Modernise government digital infrastructure

Build human capital & utilise skilled labour

- Faster recognition of overseas qualifications
- Easier vocational education pathways
- Better links between universities and industry
- Improving workforce participation

Improve efficiency & quality of care services

- Align regulation across care services to reduce duplication, improve worker mobility
- Improve coordination between hospitals, primary care & community organisations
- Invest more in prevention and early intervention

Source: Productivity Commission

The standout feature of these productivity initiatives is the estimated benefits for the Australian economy. The Budget papers argue that they will reduce regulatory burden by $10bn per year. And boost long-run GDP by around $13bn a year.

We know what is needed to kickstart productivity. We just need to get on with it. That finally seems to be happening.

Our lack of *economic resilience* was revealed by the supply chain issues following the recent oil price drama and Iran War.

Treasurer Chalmers has framed "resilience" as Australia's ability to withstand:

- geopolitical fragmentation,
- energy and supply shocks,
- ageing demographics, and
- technological disruption.

Budget measures focus on:

- Fuel and energy security via expanding national fuel reserves and a hint that domestic refining capacity is a concern.
- A new strategic reserve of critical minerals and an appetite for domestic processing.
- A major long-term lift in defence spending tied to AUKUS, advanced manufacturing and national security capability.
- A new $1 billion Economic Resilience Program through the National Reconstruction Fund to support industries facing market disruption and supply-chain shock.

A typical criticism of these sorts of measures is that they come down to government attempting to pick winners. But governments exist to deal with market failure -to provide those goods and services that the private sector can't or won't provide.

It is very hard to argue against targeting key sectors in the current environment.

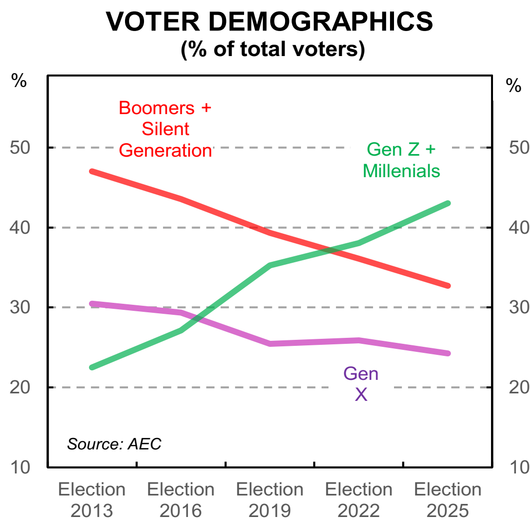
VI. Intergenerational equity

The concept of intergenerational equity is relatively new. Google search activity on the topic only appeared from 2022. The political cynic would note that the timing matches the emergence of Gen Z and Millennials as the dominant voter bloc (Fig. 22). The economic cynic would note that the idea provides a smokescreen for new taxes.

The concept is being marketed as a contribution to "fairness", an unwinding of "intergenerational theft"

as former Treasury Ken Henry once termed it and necessary for “social cohesion”.

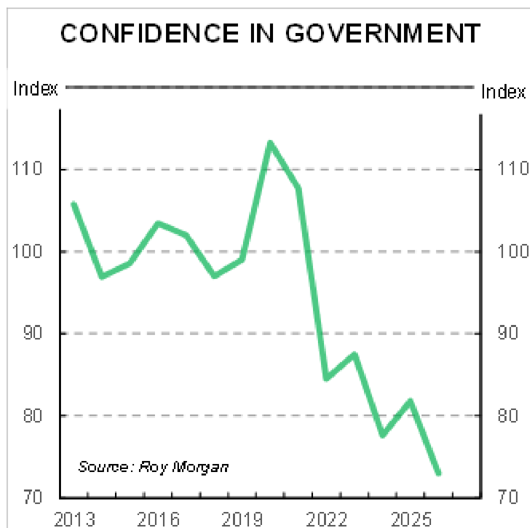
Figure 22



The central focus is changes to capital gains tax, negative gearing and the taxation of trusts.

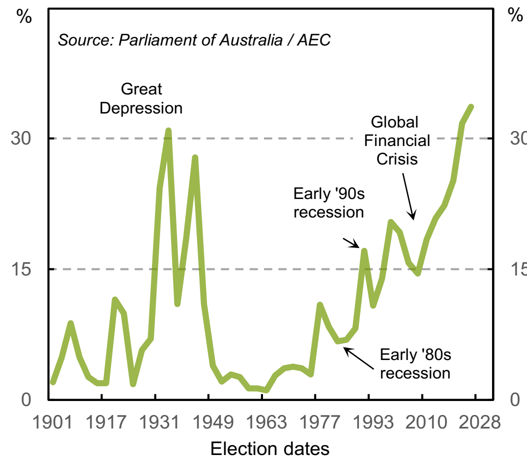
Some of these changes were explicitly and repeatedly ruled out during the 2025 election campaign. The government appears to be emboldened by voter support for the rejigging of the promised Stage 3 tax cuts.

Figure 23



One concern is that breaking promises adds to the declining trust in government (Fig. 23) and the drift towards populism (Fig. 24).

Figure 24



The decision to shift from the 50% capital gains tax discount back to taxing real gains is a case of back-to-the-future. It was the scheme in place until 1999 when the Howard government introduced the 50% discount in the name of tax simplification.

There will be winners and losers from these changes. But it is hard to be definitive given how personal circumstances vary. As a rough rule-of-thumb the average tax payer will better off under:

- The 50% discount if the asset materially outperformed inflation.
- The indexation system if inflation was very high relative to the investment return.

Budget figuring is certainly a winner. The projections show a revenue boost of $3.5bn over five years.

The shift in negative gearing towards new buildings and taxing real capital gains looks like smart policy. Anything that potentially adds to supply is a good thing. The cost is the increased complexity of working out tax obligations.

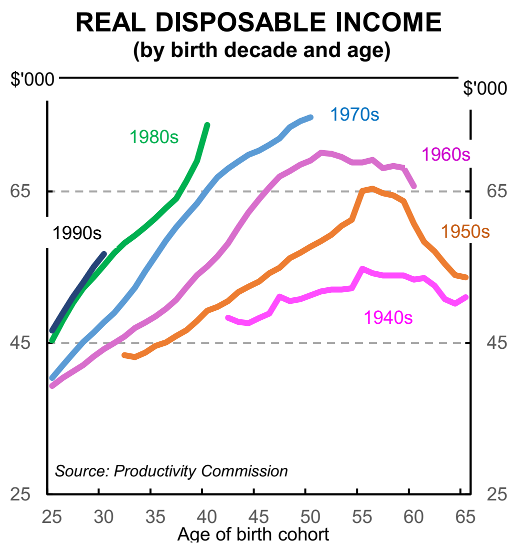
The idea that these changes are necessary to improve intergenerational equity needs to be challenged.

It could be argued that the biggest source of intergenerational theft is the large and rising public

debt that younger generations will have to service and repay.

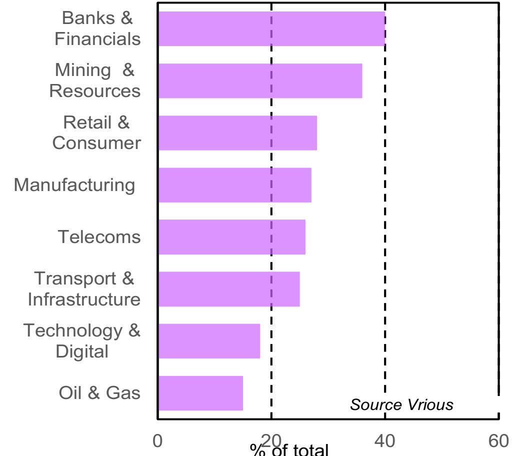
The focus is on housing ownership where younger Australians are struggling. But it is not the only metric. The trajectory of real disposable income growth, for example, for younger age groups is running ahead of those of similar age in the 1960s, 1970s and 1980s.

Figure 25



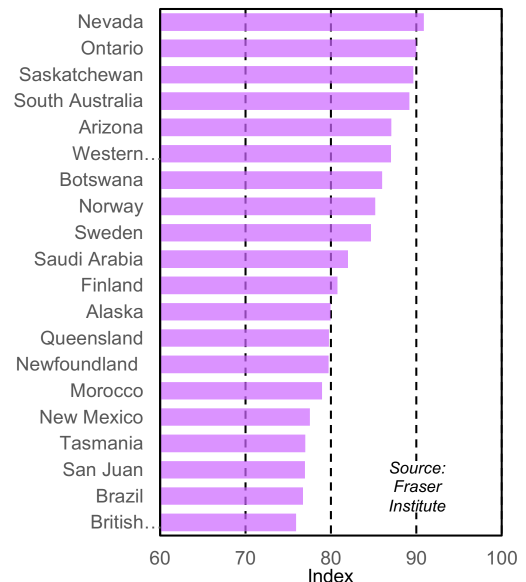
And the intergenerational lens has not been applied in other areas. The government has ruled out changing tax arrangements for resource companies despite current windfall profits. The effective tax rate paid by oil & gas companies looks out of line with profits earned (Fig. 26).

Figure 26



The broad consensus is that the "best" taxes are those applied to things people can't easily hide or move. Resources clearly fall into that category. Global mining companies may threaten to go elsewhere. But Australia has a large share of reserves in pretty much every commodity. Global miners have no choice to be invested in Australia. Surveys show that the key Australian mining States fall in the top-20 locations from an investment attractiveness perspective (Fig.27).

Figure 27



Nor has the intergenerational lens been applied to the massive wealth transfer underway as the

Boomer generation shuffle off. The available estimates put the transfer at $3-5 trillion over the next twenty years. It sounds like a fair degree of improvement in intergenerational equity is already underway.

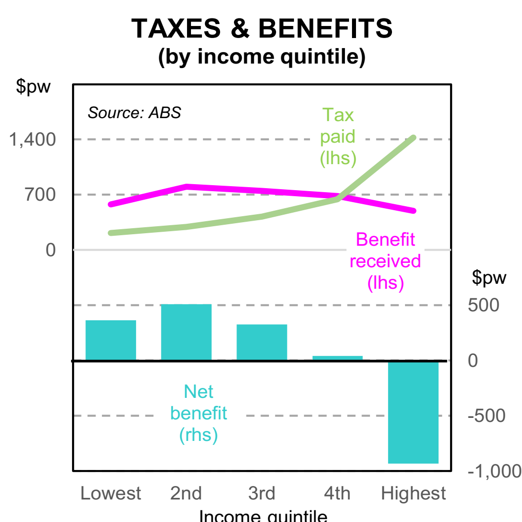
That wealth is also a major source of funding for the Bank of Mum & Dad. Digital Finance Analytics puts parental support for first-home buyers at around $35bn per year. This funding puts the Bank of Mum & Dad in the top 10 mortgage lenders. And its contributing to improving intergenerational equity.

The tax changes are presented as a reform package.

But there are more components in the tax system than just capital gains and negative gearing. And there is the benefits side of the tax/spend equation to consider as well.

A system-wide look reveals that higher income groups pay far more in tax than they receive in benefits (Fig. 28)). In fact, it is only the top income quintile (the top 20% of income earners) that pay net tax.

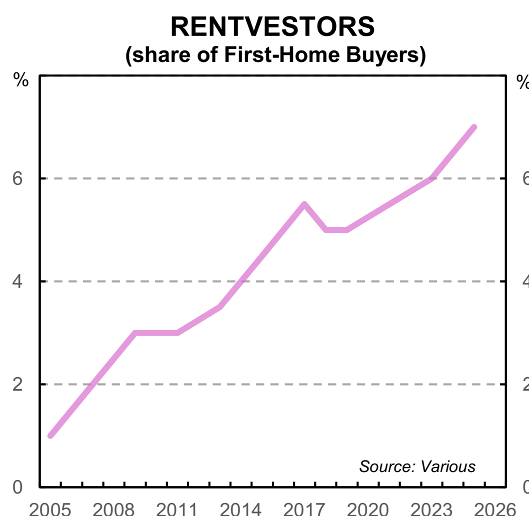
Figure 28



One risk of any tax reform is unintended consequences. And there is certainly a risk that changing housing tax arrangements may actually penalise first-home buyers.

Rentvestors are now a significant part of the housing story. It seems that first-home buyers are getting into the market by purchasing an investment property, taking advantage of the rental income and tax benefits (ie negative gearing) and only moving in when their balance sheets are in better shape. The tendency of children to remain at home for longer is the flipside of this first-home-investing trend.

Figure 29



The idea that these changes are necessary to preserve social cohesion also needs to be challenged. We are at the point where debate is about re-slicing the economic pie rather than growing the pie. And, unfortunately this idea seems to be evolving along age lines.

So this Budget features cuts to private health insurance rebates for those over 65, applying the GST to the optional services provided by aged-care facilities and that (retired) group misses out on the tax offset which is reserved for employees.

Wealth does increase with age. Older age groups have had longer to accumulate assets. But not all older people are rich.

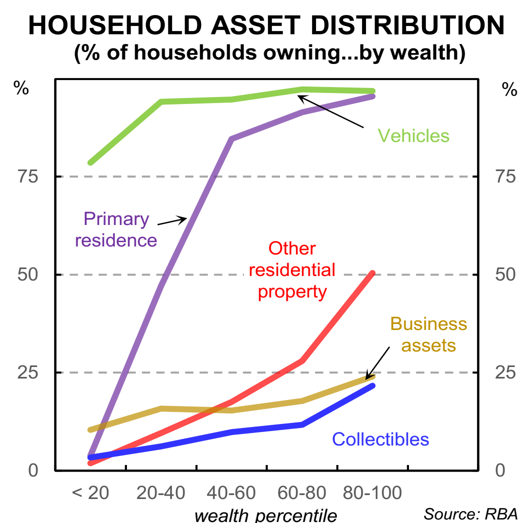
The latest *Council on the Aging* report on older Australians shows:

- 28% of those over 50 are "wealthy";
- But 25% are in poverty; and

- 54% of those fully or partially retired rely on the Age Pension or other government benefits as their primary income source.

We also have to acknowledge the real world here. It is a truism that the rich have more of everything. Who would've thought (Fig. 30)!

Figure 30



Meanwhile, I'm off to become more productive and resilient!

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