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FEDERAL REVENUES APPEAR TO BE DRYING UP MORE THAN EXPECTED

By Key Measure, Revenues May Hit Lowest Level in About Four Decades, Even Before New Tax Cuts

By Isaac Shapiro

Treasury data on how much revenue was collected through the end of April are now available. These data, which reflect final Treasury data through the end of March and an analysis of preliminary data through the end of April, show the following:

- Federal receipts for the current fiscal year are running substantially below receipts for the previous fiscal year. From October 2002 through April 2003 (the first seven months of fiscal year 2003), total federal receipts were $59 billion below what they were during the comparable seven months of fiscal year 2002. (All figures in this analysis are in "nominal" terms; they are not adjusted for the effects of inflation.)

- Revenues appear to be falling even further short of the Congressional Budget Office's official projection of expected revenues. CBO has projected that federal revenues would be *$38 billion higher* in fiscal year 2003 than in fiscal year 2002. Yet so far, revenues have been *$59 billion lower* this year, yielding a gap to date of nearly $100 billion. Revenues would have to grow in a sharp and almost unprecedented fashion for this gap to be made up over the next five months.[1] It thus seems very likely that CBO's estimate of revenues for this year will prove too high.

Revenue decline from 2002 to 2003, first seven months	-$59 billion
CBO projected increase for all of 2003	$38 billion
Gap	-$97 billion

- If federal revenues for the remainder of the fiscal year are the same as for the last five months of fiscal year 2002 (that is, assuming no further drop in receipts), federal revenues are on course to hit a 44-year low as a percentage of the economy. Instead of CBO's current projection that revenues will equal 17.6 percent of the economy in 2003, receipts as a percentage of the economy would

[1] For the gap to be closed entirely, receipts for the remaining five months of 2003 would need to be about 13 percent higher than receipts for the last five months of 2002. An examination of trends since 1982 indicates that such a percentage increased occurred only once, in 2000 when receipts boomed throughout the year.

> drop to 16.7 percent. This would be the first time this measure has been below 17 percent since 1959.
>
> Under a somewhat optimistic scenario that assumes the trend over the remainder of the year departs from the trend from the first seven months of the year and that half of the nearly $100 billion gap below CBO's projection is closed in the coming five months, revenues as a percent of the economy would equal 17.1 percent of the economy in 2003. This would be the lowest level since 1965.

Around May 9, CBO will release its analysis of the Treasury data through April. Typically, this is the time when CBO indicates whether revenues are ahead of or behind its projections. CBO waits until the April data are available before discussing modifications to its projections, because it is not until the income tax season is over that a solid reading of revenue patterns can be made. When CBO releases its analysis, one may be able to estimate with more precision how much revenues in 2003 are coming in below what CBO predicted, and whether the fall might be so large that revenues will hit their lowest level as a percent of the economy in 38 years or perhaps 44 years, even before considering any further decline in revenues due to a tax cut.

The current evidence on the degree to which revenues have already fallen suggests that Congress should proceed with caution as it formulates new tax cuts. The evidence indicates both that the economy may already be receiving a larger stimulus than official projections indicate and that receipts may be falling to levels so low that questions about the adequacy of the revenue base are pertinent.

The Estimates

The most recent Monthly Treasury Statement contains information about federal receipts through the end of March 2003, which represents the first half of fiscal year 2003. The Treasury data indicate that federal receipts for the first six months of fiscal 2003 equaled $825 billion, or $54 billion below the $879 billion in receipts collected during the first six months of fiscal 2002.

The monthly Treasury figures are based on daily Treasury figures that the Department releases with a one-day lag; that is, receipts for Wednesday April 30, 2003 were released on Thursday May 1, 2003. An analysis of the daily Treasury figures indicates that revenues in April 2003 were $5 billion lower than revenues in April 2002. Due to revisions in the figures that sometimes occur, the final Treasury figures for the month of April may differ somewhat from this tabulation of the daily figures.

Adding the $5 billion drop in revenues in April to the $54 billion drop through March yields the estimate that revenues for the first seven months of 2003 are $59 billion lower than revenues for the first seven months of 2002. If revenues for all of 2003 come in lower than for all of 2002 that would be the third year in a row in which revenues declined on a nominal basis. The last time revenues declined for three consecutive years was from 1920 to 1923.

Receipts as a Percent of the Economy

In January and March 2003, CBO estimated that tax receipts would equal 17.6 percent of the economy in fiscal year 2003.[2] As the table at the end of this analysis indicates, this level is consistent with the levels of the early 1980s and 1990s. These time periods are appropriate comparisons because receipts tend to drop during economic downturns and to rise during recoveries.

CBO projected that revenues in 2003 would be $38 billion higher than in 2002, under current law. As noted, so far revenues are $59 billion lower than in 2002.

- If revenues for all of 2003 are $59 billion below revenues for all of 2002, this would amount to a total difference of $97 billion ($38 billion plus $59 billion) from CBO's projection. Revenues as a percent of the economy would equal 16.7 percent, the lowest share since towards the end of the Eisenhower Administration.

- If the $97 billion gap is cut in half by the end of the year, revenues would equal 17.1 percent of the economy, the lowest level in 38 years. For the gap to be cut in half, revenues would have to grow considerably relative to 2002, a somewhat optimistic projection that would depart from the trend for the first seven months of the year.

While the decline in revenues partly reflects the decline in the economy, it also reflects the tax cuts that have already been enacted during the Bush Administration. In total, these tax cuts will reduce revenues in 2003 by $126 billion, based on CBO's estimates of the cost of the legislation.[3] Without the tax cuts, revenues as a percent of the economy would not be close to being at their lowest level since either 1959 or 1965.

[2] This calculation reflects both CBO's projection of receipts and its projection of the size of the economy, or the Gross Domestic Product. With actual GDP information available for the first half of fiscal 2003, CBO's GDP projection is essentially right on the mark. So for the various calculations used in this analysis, CBO's GDP projection for the year is used.

[3] Even if one assumes the level of positive feedback on the economy from the 2001 tax cut that was estimated by the President's Council on Economic Advisors, the tax cuts will reduce revenues by an estimated $109 billion in 2003. For a discussion of the possible economic feedback and the CEA estimates, see the Center on Budget and Policy Priorities publication, "Are Tax Cuts a Minor or Major Factor in the Return of Deficits? What the CBO Data Show," February 12, 2003.

Federal Receipts as a Share of Gross Domestic Product, 1950-2003			
1950	14.4%	1978	18.0%
1951	16.1	1979	18.5
1952	19.0	1980	18.9
1953	18.6	1981	19.6
1954	18.4	1982	19.1
1955	16.6	1983	17.5
1956	17.4	1984	17.4
1957	17.7	1985	17.7
1958	17.3	1986	17.5
1959	16.1	1987	18.4
1960	17.8	1988	18.1
1961	17.7	1989	18.3
1962	17.5	1990	18.0
1963	17.8	1991	17.8
1964	17.6	1992	17.5
1965	17.0	1993	17.6
1966	17.3	1994	18.1
1967	18.3	1995	18.5
1968	17.6	1996	18.9
1969	19.7	1997	19.3
1970	19.0	1998	19.9
1971	17.3	1999	20.0
1972	17.5	2000	20.8
1973	17.6	2001	19.9
1974	18.3	2002	17.9
1975	17.9	2003est.	17.6*
1976	17.2	2003est.	17.1**
1977	18.0	2003est.	16.7***

*CBO baseline
**CBPP estimate if revenues fall $48.5 billion below the baseline.
***CBPP estimate if revenues fall $97 billion below the baseline.