

Revenue Blow Out

The U.S. Treasury Department reported a gusher of tax revenue last week. Tuesday alone, the Treasury received \$48.7 billion from *individual* taxpayers as their final tax payment for 2006, an all-time single-day record, and one-third higher than the same day last year.

Based on information available through Friday, we estimate federal receipts at about \$390 billion in April. This would be the largest tax take for any month in American history, up 25% versus last April, and up 18% versus the previous record high in April 2001.

With incomes and profits growing rapidly, the U.S. budget deficit will fall to about \$145 billion during the twelve months ending in April. To put this in perspective, the deficit was \$455 billion as recently as three years ago (the twelve months through April 2004).

These trends increase our confidence in the lonely forecast we made back in early February that the budget deficit would drop to \$115 billion for the 2007 fiscal year, and disappear in Fiscal 2009, possibly before. In contrast, the Congressional Budget Office estimates a deficit of \$177 billion this year, with the White House at \$244 billion. Expect major revisions to these numbers.

Our budget forecasts are based on reasonable projections. For example, on the revenue side, we have May receipts down 2.6% versus last May. (Due to calendar quirks some of the April receipts this year would normally have arrived in May.) Beyond that, we have revenue growing between 8.5 – 9% annually through 2009, consistent with our expectation of a strong economy and also with historical patterns from the expansions of the 1980s and 1990s. Revenue grew at a 13.2% rate in Fiscal 2005 and

2006, and should grow at a 9.1% rate this year despite temporary “patches” for the Alternative Minimum Tax. Our projections assume these AMT patches continue, so we are not relying on many more taxpayers being subject to the AMT to generate our revenue numbers.

On the spending side, so far this fiscal year outlays are up less than 3%. We assume they accelerate to a 4.5 – 5% annual growth rate through 2009.

Our deficit projections show that the US is slightly ahead of the actual 1990s deficit path. In 1996 – almost six years into recovery – the deficit was still 1.4% of GDP. The first surplus arrived in 1998. We expect the deficit to be just under 1% of GDP for Fiscal 2007 (almost six years into the recovery), with surpluses arriving in 2009 or earlier.

As in the 1990s, revenue is being lifted by a productivity-driven surge in incomes, profits, and rising equity prices. As people earn higher incomes, a larger share of their income gets taxed at higher marginal rates – a tax hike without new legislation. Those who argued that the tax cuts in 2001-03 would create deficits as far as the eye could see are being proven wrong. And, unlike the 1990s, the budget will be balanced without the help of a post-Cold War “peace dividend.”

Unfortunately, the surpluses we will achieve will not be permanent. Social Security and Medicare are still problems. Massive spending cuts or tax hikes (or both!) may hit us in a few decades. But for the next several years, as long as spending is restrained, revenue growth will continue to surge and the budget picture will improve faster than conventional wisdom believes – this, in turn, will undercut the push by many politicians to hike tax rates back to pre-2001 levels.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-30 / 7:30 am	Personal Income - Mar	+0.6%	+0.7%	+0.7%	+0.7%-R
7:30 am	Personal Spending - Mar	+0.5%	+0.7%	+0.3%	+0.7%-R
8:45 am	Chicago PMI - Apr	54.0	56.0	52.9	61.7
9:00 am	Construction Spending - Mar	+0.2%	-0.5%	+0.2%	+1.5%-R
5-1 / 9:00 am	ISM Index - Apr	51.0	51.4		50.9
<i>sometime</i>	Domestic Auto Sales - Apr	5.2 Mil	5.3 Mil		5.1 Mil
<i>during the day</i>	Domestic Truck Sales - Apr	7.3 Mil	7.2 Mil		7.2 Mil
5-2 / 9:00 am	Factory Orders - Mar	+2.1%	+1.9%		+1.0%
5-3 / 7:30 am	Initial Claims - Apr 28	323K	325K		321K
7:30 am	Q1 Non-Farm Productivity	+0.8%	+0.5%		+1.6%
7:30 am	Q1 Unit Labor Costs	+4.0%	+1.6%		+6.6%