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COVID-19: Early revenue impact, April 2020

PBO Publication 13 of 2020

This note analyses the revenue outturns contained in the Department of Finance's *Fiscal Monitor* publication for March (published on 2nd April). It provides additional context to these figures in light of the onset of the COVID-19 pandemic and explores the potential impact of the crisis for the ongoing stability of the public finances.

Key Points

- The COVID-19 pandemic has had a minimal impact on the amount of tax revenue collected to end-March. This is to be expected, as administrative restrictions were only introduced in the latter half of the month;
- However, some early impacts of the pandemic are evident. While March is a VAT due month, receipts were €1.1 billion (-50.6%) below monthly profile, due to the introduction of revenue forbearance measures in response to the crisis. Excise was also below monthly profile, by 21.5%;
- Income Tax was ahead of monthly profile by €75 million (or 4.7%). The employment impact of COVID-19 restrictions on receipts will be clearer in future iterations of the *Fiscal Monitor*, as most non-essential businesses closed towards the end of March. The number availing of COVID-19 related income supports was 308,141 at end-March. However, this number will likely rise significantly in the coming weeks;
- Corporation Tax was €39 million (or 15.5%) ahead of profile. Most Corporation Tax revenue is collected across May, June and November, and the amount collected in 2020 will be partially impacted by activity in 2019. In addition, Corporation Tax revenue is driven by three key sectors – *Manufacturing, Financial and Insurance Activities, and Information and Communications*. Of these, receipts for *Manufacturing* alone are generally more than double the amount collected by the most impacted sectors (*Wholesale and Retail Trade, and Accommodation and Food Services*);
- On a monthly basis, total tax revenue was €1.1 billion below profile (or 22.5%). In cumulative terms, tax revenue is €788 million (or 5.7%) below profile as of end-March, buoyed by a relatively strong performance in January and February.
- On an annual basis, cumulative tax revenue was €138 million (or 1.1%) higher than in the same period last year;
- An Exchequer deficit of €2.5 billion was recorded as of end-March (compared to a deficit of €966 million in the same period last year). This will deteriorate significantly more in the coming months.

Background – Tax revenues pre-COVID-19

The COVID-19 pandemic is a significant threat to the stability of the public finances.

The policy response to date, has been to limit the transmission of the disease by effectively closing certain sectors of the economy, and by reducing or limiting the activity in others. On March 12th, the Taoiseach recommended the cancellation of mass gatherings and announced the closure of schools, colleges and childcare facilities. Since then, additional restrictions aimed at limiting the spread of the virus through social distancing, have been implemented. These restrictions include the closure of pubs and hotel bars (on March 15th), and advice against all non-essential travel outside of the home and the closure of public amenities and non-essential retailers (on March 27th). These measures are in effect until April 12th (at the earliest). The fiscal impact of these measures, and the long-term implications for the public finances, will depend on the longevity of the temporary closures, the ongoing policy response, and the behavioural response of the public once the restrictions have been lifted.

The latest fiscal forecasts (published for the first time in the *Fiscal Monitor* for March)[1] pre-date the onset of the COVID-19 pandemic and estimate **€63.5 billion** in tax revenue for 2020. This consists of:

- €24.7 billion in Income Tax;
- €15.9 billion in VAT;
- €11.8 billion in Corporation Tax; and,
- €6.3 billion in Excise.

These forecasts are an upward revision to those underpinning Budget 2020 (in October 2019), which assumed a disorderly Brexit for 2020. However, these estimates will be subject to significant further revision in light of the COVID-19 pandemic.[2]

COVID-19 – Economic impact

The COVID-19 pandemic has caused unprecedented disruption to economic activity, with large-scale business closures and job losses. Fiscal measures totalling €6.7 billion have been announced to date. However, significant additional spending may be required (depending on the duration of the crisis) at a time when tax revenues are likely to fall substantially below expectations. As a result, a sizeable deficit should be expected for 2020, requiring significant levels of borrowing. A surplus of 0.7% of GDP was originally expected for 2020 (approximately €2.5 billion).

The Economic and Social Research Institute (ESRI)[3] has modelled the impact of a scenario involving a disruptive 12-week pandemic period (occurring in Q2), in which consumption, investment and exports are heavily impacted, before a domestic and global recovery in the second half of the year. This scenario projects that unemployment would rise to 16.5% by Q3, before ending the year at 10.7%. It further projects a deficit for 2020 of 4.5%, with negative GDP growth at -7.1% (a 10.4 percentage point reduction relative to their December forecast). A similar scenario is modelled by the Central Bank. Under a three-month containment period and gradual roll-back of restrictions, GDP is estimated to contract by 8.3% (growth of 4.8% was predicted in February). Similarly, personal consumption is estimated to fall by 9% (growth of 2.7% was predicted in February), while unemployment is estimated to reach 24.7% in Q2 before ending the year at 10.5%. The Central Bank further predicts a deficit of 6% for 2020, with debt-to-GDP (GNI*) rising to 66% (112%).

Live Register data for March[4] shows that 308,141 people are availing of COVID-19 related income supports (including 283,037 for the Pandemic Unemployment Payment and 25,104 for the Wage Subsidy). These numbers are likely to increase in the coming weeks. In a previous publication, the PBO estimated that approximately 492,000 employees will be unable to work as a result of closures in the most impacted sectors.[5] Analysis by the Central Bank suggests that this number could be as high as 650,000.[6] Furthermore, in costing these measures, the Department of Finance has estimated that as many as 800,000 individuals could ultimately claim one of the two supports.[7]

The long-term economic and fiscal impact of the pandemic will depend on the extent to which affected individuals can return to work once the public health crisis has subsided.

1 Fiscal Monitor, Department of Finance, 2 April 2020.
2 The Department of Finance has indicated that monthly tax profiles will be recalculated as part of the production of the *Stability Programme Update* for 2020.
3 Quarterly Economic Commentary, Economic and Social Research Institute, Spring 2020.
4 CSO – Live Register, March 2020.
5 PBO Publication 9 of 2020 – Employment in Sectors Most Exposed to the COVID-19 Pandemic, 30 March.
6 Quarterly Bulletin, QB2 – April 2020, Central Bank of Ireland.
Note: the Central Bank assume a broader range of impacted sectors than PBO (e.g. essential retail and construction).
7 PBO Publication 7 of 2020 – Ireland's fiscal response to COVID-19, 25 March.

Fiscal Monitor – March 2020

The *Fiscal Monitor* for March provides an insight into the early and initial impact of COVID-19 on the public finances.[8] An overview of revenue developments by tax category is given below, with a particular focus on the four largest tax heads (Income Tax, VAT, Corporation Tax and Excise, which account for approximately 93% of total tax revenue).

Key revenue developments

VAT

March is a VAT due month. However, just €1.1 billion was collected. This is significantly less than anticipated (by 50.6%). An additional €1.1 billion was expected in the month. In cumulative terms, receipts are down 17% on the same period last year.

The Department has indicated that this is not due to a fall in consumption in the month, but rather, revenue forbearance introduced in March regarding the payment of VAT in respect of consumption in Q1.

The current restrictions are in place until April 12th (at the earliest). The impact of the effective shutdown of non-essential business in the second half of March, as well as an uncertainty-driven[9] slowdown in the first half of the month (as anxieties related to COVID-19 took hold and dampened consumer sentiment), should be prominent in subsequent *Fiscal Monitors*. Early indicators point to a slowdown in consumption for the month (the volume of credit and debit card transactions declined significantly in March, estimated to be 28% less than expected).[10]

Personal consumption is a key driver of VAT revenue and has been impacted by both a demand and a supply shock as a result of the pandemic. Business closures are causing job losses and wage reductions which depress the level of demand, while administrative restrictions are limiting spending on nonessential goods and services. This will persist throughout the pandemic period. The heightened uncertainty (particularly regarding earnings and employment prospects) during the crisis and beyond (once restrictions have been lifted), is also likely to drive precautionary saving and further limit spending.

Under a 12-week pandemic scenario, the ESRI estimates negative consumption growth of -3.8% for 2020 (a contraction of 6.3 percentage points relative to the December forecast). A similar scenario modelled by the Central Bank predicts a contraction in personal consumption of 11.7 percentage points, relative to their February forecast.

At a micro level, the ESRI model a reduction in the weekly spending of the average Irish household during the pandemic period, of €205 (from €837 to €632). Using a similar approach, the PBO estimates a reduction in the weekly VAT contribution of the average household of €34 (or 53%).[11]

Income Tax

€1.7 billion was collected from Income Tax in March, marginally above profile (by €75 million or 4.7%). In cumulative terms, receipts are 13.5% higher than in the same period last year.

8 It is important to note that, the first set of restrictions was announced on March 12th. Notwithstanding the uncertainty surrounding the first two weeks of March, and the consequences for economic activity during that time, revenues for March will likely be buoyed by the relatively normal level of activity taking place in the first half of the month.

9 Irish Consumer Sentiment Index, KBC, 20 March 2020.

10 Quarterly Bulletin, QB2 – April 2020, Central Bank of Ireland.

11 This follows the ESRI's analysis (in the Quarterly Economic Commentary, Spring 2020) which uses data from the Household Budget Survey to assess the potential impact of the COVID-19 pandemic on the consumption pattern of the average Irish household. Generally, non-essential spending is set to zero, with increases in essential spending (such as medical expenses and food consumed at home). We make an upward revision to the amount spent on fuel and lighting (to account for the increase in time spent inside the home during the pandemic). Relevant VAT rates are then applied to each category of spending. For context, we estimate that in a non-pandemic week, the average household contributes €65 in VAT (or €3,381 annually).

The employment impact of COVID-19 will likely appear in April's Income Tax receipts, with most nonessential businesses closing towards the end of March. The numbers availing of the Pandemic Unemployment Payment was 283,037 at end-March. A further 25,104 are availing of the Wage Subsidy scheme.[12] However, these numbers will likely rise significantly in the coming weeks.

The PBO has estimated that, to date, 492,000 employees will be unable to work as a result of closures in the most impacted sectors,[13] while the Central Bank suggests that this number could be as high as 650,000. The Department has estimated that as many as 800,000 individuals could end up claiming either measure.[14] Under their 12-week pandemic scenario, the ESRI predicts negative employment growth of -7.6% for 2020 (a contraction of 10.4 percentage points relative to their December forecast). Under a similar scenario, the Central Bank estimates that unemployment could reach 24.7% in Q2 before finishing the year at 10.5% in Q4. The impact of COVID-19 on Income Tax revenue in the medium-term, will depend on the duration of the temporary closures, and the ability of those availing of pandemic-related income supports to return to work once the crisis subsides.

It is worth noting that most Income Tax revenue is paid by those earning over €75,000 (roughly 63% of revenue, as of 2017).[15] This cohort of earners is less likely to be directly impacted by COVID-19 related closures (notwithstanding potential wage reductions as a result of the crisis). As outlined in a previous PBO publication, average earnings in the most impacted sectors (i.e. those directly affected by closures such as hospitality, retail and recreation) are generally below the national average.[16]

On a sectoral level, the employees of firms that are likely to be least impacted by closures (such as Manufacturing, Financial and Insurance Activities, and Information and Communications) contribute roughly 43% of Income Tax receipts, while those working in the most impacted sectors (and those most likely to be availing of emergency income supports, such as Wholesale and Retail Trade, and Accommodation and Food Services) contribute roughly 19%.[17]

Corporation Tax

€403 million was collected from Corporation Tax in March..[18] This was €39 million (or 15.5%) more than expected. Cumulatively, Corporation Tax continues to perform strongly (68.3% above profile, and 66% higher than in the same period last year). As yet, there is no apparent COVID-19 related impact on Corporation Tax receipts. The majority of Corporation Tax is collected across May, June and November, and the amount collected in 2020 will in part be impacted by payments made in 2019.

Corporation Tax revenue is generally driven by three key sectors – Manufacturing, Financial and Insurance Activities, and Information and Communications. These three sectors account for 71% of receipts (as of 2018) and are less likely to have been impacted by COVID-19 related closures. Receipts for Manufacturing alone (at €3.2 billion) were 2.3 times the amount collected by sectors most impacted by the closures (Wholesale and Retail Trade, and Accommodation and Food Services, contributed €911 million or 11% of total receipts).[19]

Corporation Tax has been characterised by sizeable outperformances in recent years. The ongoing impact of COVID-19 on receipts through 2020 will largely depend on the global scale of the crisis. Firms involved in high-tech manufacturing may not be as adversely affected in the short-term, compared to firms that are subject to closures, such as in retail and hospitality. However, the medium-to-long term profitability of these firms will depend on the extent to which the pandemic can be curtailed in key export markets, and on the potential for

12 CSO – Live Register, March 2020.
13 PBO Publication 9 of 2020 – Employment in Sectors Most Exposed to the COVID-19 Pandemic, 30 March.
Note: the Central Bank assume a broader range of impacted sectors than PBO (e.g. essential retail and construction).
14 PBO Publication 7 of 2020 – Ireland's fiscal response to COVID-19, 25 March.
15 Income Tax statistics, Revenue Commissioners.
16 PBO Publication 9 of 2020 – Employment in Sectors Most Exposed to the COVID-19 Pandemic, 30 March.
17 Revenue Commissioners, May 2019.
18 The Department stated that the majority of this was collected from large companies. In 2018, the top ten Corporation Tax contributors paid 45% of all Corporation Tax revenue (Revenue Commissioners, May 2019).
19 Revenue Commissioners, May 2019.

ongoing disruptions to global supply chains and trading relationships.

Excise

€402 million was collected from Excise in March. This was €110 million less than expected (-21.5%). In cumulative terms, receipts are down 6.7% on the same period last year.

Similar to VAT, Excise is a transaction-based tax. However, it is generally levied on goods for which there is relatively inelastic[20] demand (i.e. fuel, tobacco, and alcohol). While receipts will likely be impacted by a general fall in consumption (e.g. due to the closure of bars and pubs), this impact will be less pronounced than for VAT receipts.

Capital Taxes, Motor Tax and Customs

For Stamp Duty and Capital Gains Tax, €153 million was collected in March (a combined 37% above profile). Cumulatively, these taxes are 12.5% above profile (and 16.8% higher than in the same period last year).

€13 million was collected for Capital Acquisitions Tax (25.4% below the monthly profile). Motor Tax was broadly in line with the monthly profile at €83 million (but 4.7% lower in cumulative terms relative to last year). Customs revenue was also in line with the monthly profile at €26 million (but 12.9% lower in cumulative terms relative to last year).

Stamps and Customs in particular, will likely be heavily impacted by the COVID-19 restrictions in the coming weeks (e.g. the negative implications for housing transactions, and financial transactions, as well as the adverse implications of the global shutdown for trade).

20 This means that consumption is relatively resistant to changes in income and prices.

Chart Pack 1: Cumulative performance against profile (€millions) Q1 2020, largest taxes

Figure 1a. VAT

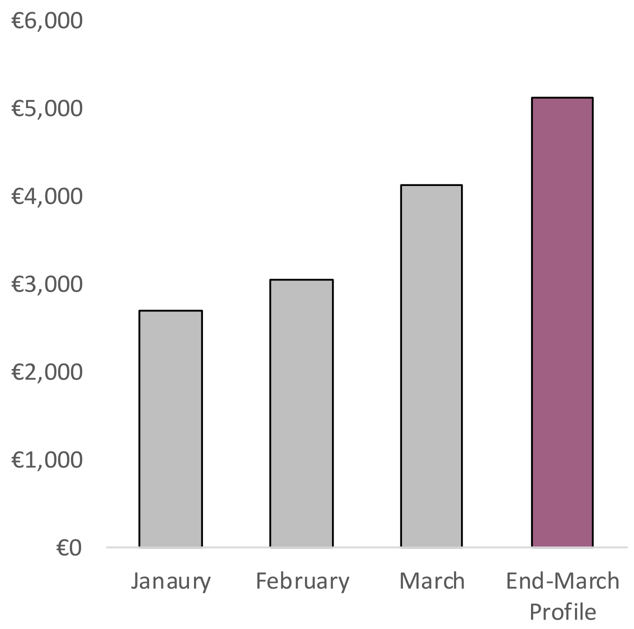
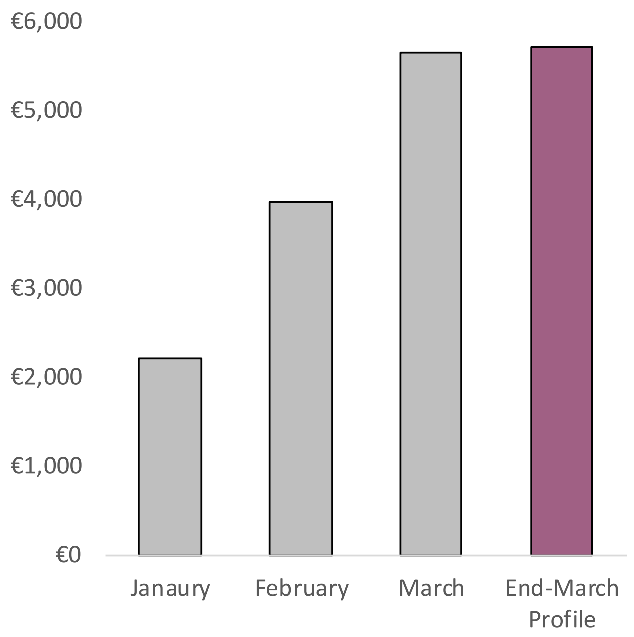


Figure 1b. Income Tax



Source: Fiscal Monitor, Department of Finance, April 2020.

Figure 1c. Corporation Tax

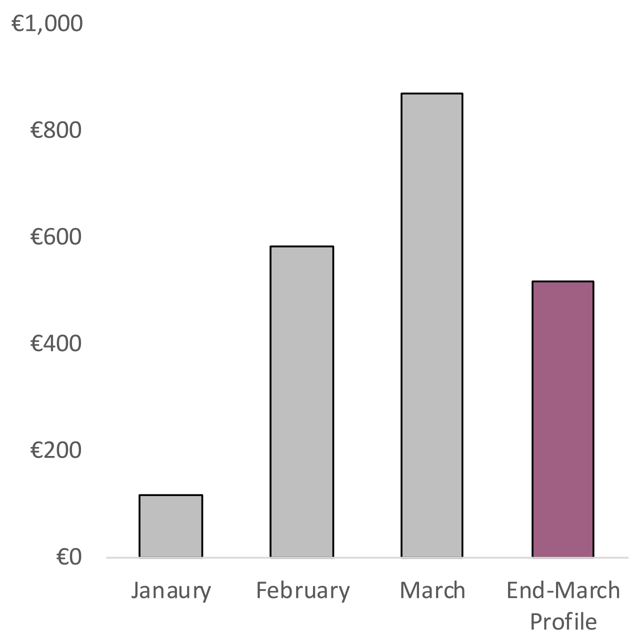
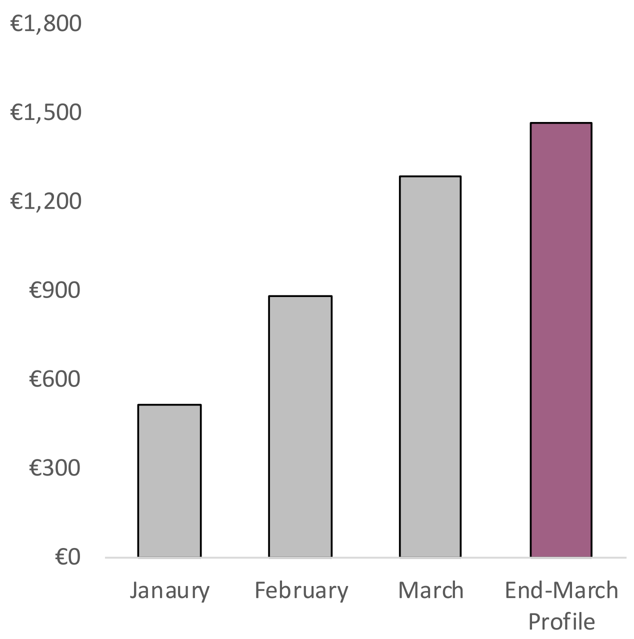


Figure 1d. Excise



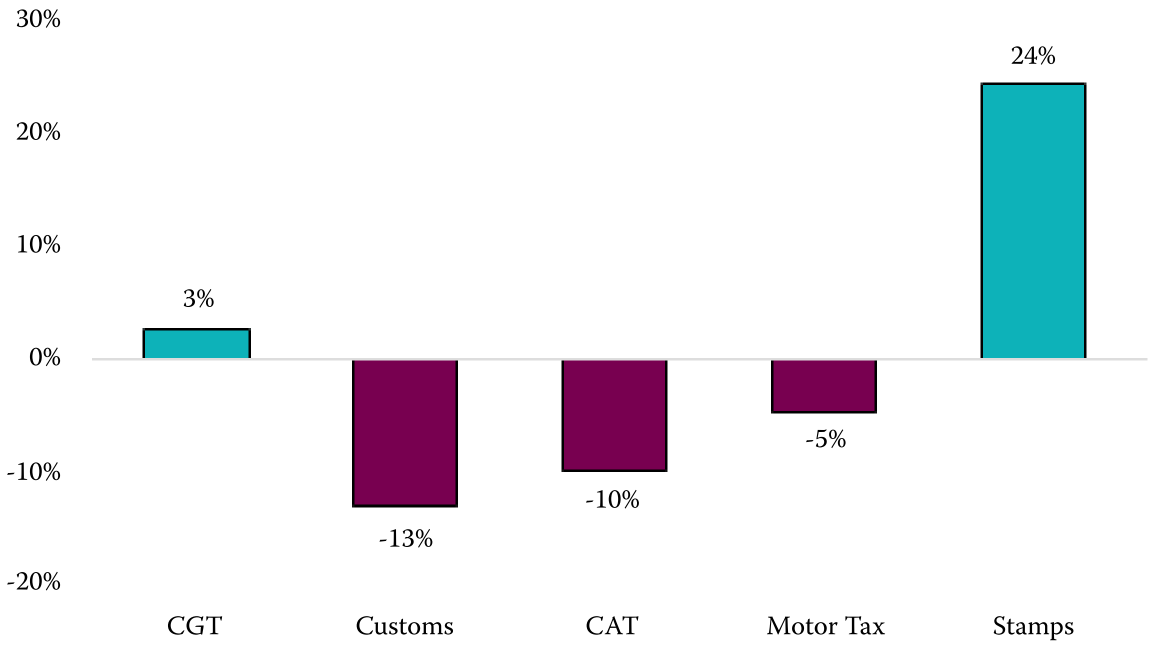
Source: Fiscal Monitor, Department of Finance, April 2020.

Chart Pack 2: Cumulative year-on-year performance, all taxes

Figure 2a. Cumulative performance: Q1 2020 versus Q1 2019, largest tax categories

Source: Fiscal Monitor, Department of Finance, April 2020.

Figure 2b. Cumulative performance: Q1 2020 versus Q1 2019, remaining tax categories

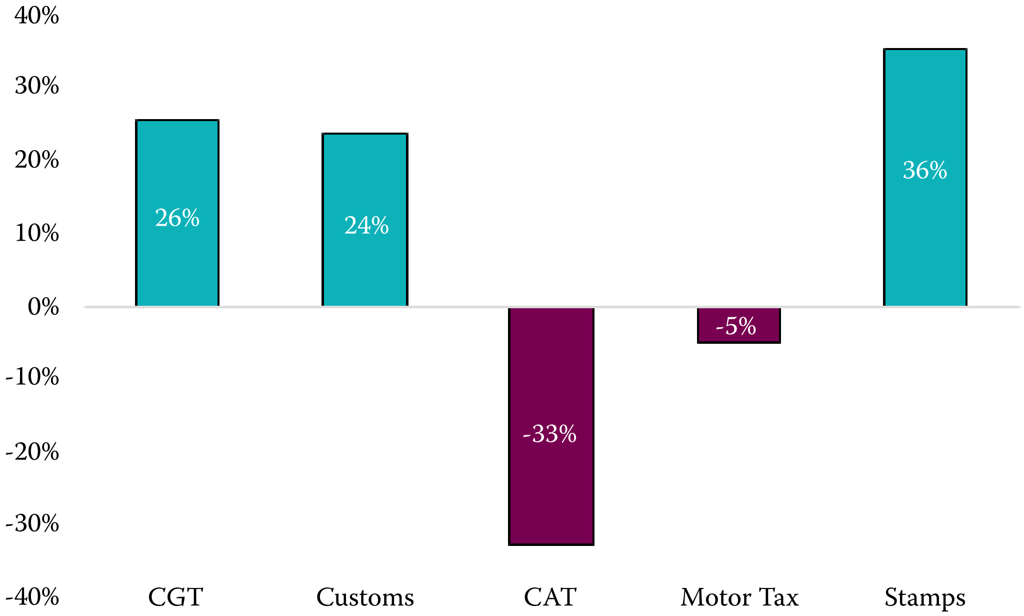


Source: Fiscal Monitor, Department of Finance, April 2020.

Figure 2c. Monthly performance: March 2020 versus March 2019, largest tax categories

Source: Fiscal Monitor, Department of Finance, April 2020.

Figure 2d. Monthly performance: March 2020 versus March 2019, remaining tax categories



Source: Fiscal Monitor, Department of Finance, April 2020.

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