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Tax revenue and employment level in Nigeria

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ABSTRACT

Employment levels are of concern in Nigeria, with unemployment and underemployment rates weakening the country's economic performance and social order. The literature identifies employment levels among the key indicators of a country's economic health and agrees that the relationship between tax revenue (personal income tax, corporate income tax, value-added tax, petroleum profit tax) and employment levels is of interest to policymakers because taxation is critical in mobilizing funds for government investment. However, the effect of tax revenue on employment levels in Nigeria has remained contentious, as the available literature provides divergent views. Hence, this study examined the effect of tax revenues on employment levels in Nigeria, based on 43 years (1980–2023) of data sourced from the Central Bank of Nigeria and the World Bank. The study deployed the Autoregressive Distributed Lag (ARDL) model of econometric procedures. Tax revenue exerted inconsistent effects on employment levels in the short and long run. There is a mismatch between the country's tax structure and current economic realities. Reforms should be implemented to align the tax structure with current economic conditions. Additionally, the economic environment should be assessed for effective future tax reforms, and existing tax-based project funding arrangements should be reviewed.

Contribution/Originality: This study examined the effect of tax revenues on employment levels in Nigeria, employing the Autoregressive Distributed Lag (ARDL) model of econometric methodology for analysis. The study is highly relevant to Nigeria, considering the ongoing debate about the usefulness or otherwise of the government's planned reform of Nigerian tax laws and tax administration mechanisms.

1. INTRODUCTION

Employment levels are among the key indicators of a country's economic health. In Nigeria, high unemployment and underemployment rates have long been concerns for policymakers and stakeholders, as they hinder economic progress and social stability. Shuaib and Ndidi (2015) noted that the creation of economic and social capitals that result in the growth of national output through increased employment opportunities and poverty reduction is a significant aspect of economic development. In the same vein, Ayeni and Omodero (2022) emphasized that the desire for strong economic performance is not just an ambition of countries but a necessity that could impact employment prospects, income distribution, and the overall living standards of the people. Likewise, Palmtag (2024) stated that employment levels continue to be one of the measures of economic development that show how well an economy is able to create jobs for its workforce.

There is a complex relationship between tax revenue and employment levels. Tax policy changes may curtail job creation by imposing financial burdens on businesses and individuals. On the other hand, tax policy changes may enhance government tax revenue and cause increased government spending, which is capable of promoting job creation. An understanding of this relationship is imperative to be able to design tax strategies that support job creation. Jadranka, Milenković, and Kalaš (2019) highlighted the importance of defining tax levels and shares to optimize economic performance. Ranđelović (2022) noted that the primary aim of taxation is mobilizing revenues to fund government services, which ensure fiscal sustainability, long-term economic growth, and create employment opportunities for the people. It is estimated that a tax revenue of 15% of gross domestic product (GDP) is needed to boost economic development, as that level of funds could support public investments that promote stability and improve employment levels (Junquera-Varela & Haven, 2018). Nevertheless, the mobilization of tax revenue for financing the government's developmental activities in Nigeria has been a challenge over the years due to various inactions by taxpayers and tax officials (Adegbie & Fakile, 2011). Furthermore, the Internation Monetary Fund (IMF) (2023) reported that Nigeria's very low revenue-to-GDP ratio has made the country's financial position very weak. Similarly, Agusto & Co (2023) stated that Nigeria's tax-to-GDP ratio was below what was required for long-term economic growth.

The impact of tax revenue on employment levels in Nigeria has remained a subject of debate, as studies have continued to offer different viewpoints and providing no finality on whether the relationship is positive and significant (Anichebe, 2019; Domguia, Pondie, Ngounou, & Nkengfack, 2022; Obaretin & Uwaifo, 2020; Ofoegbu, Akwu, & Oliver, 2016) negative or insignificant (Balasoiu, Chifu, & Oancea, 2023; George-Anokwuru, 2022; Osirim, George, & Chukwu, 2022) and mixed effect (Gbenga & Nicholas, 2023; Otekunrin et al., 2023) thereby, confirming the existence of a gap requiring further examination. Hence, the study's objective was to examine the effect of tax revenues on employment levels in Nigeria.

2. LITERATURE REVIEW

2.1. Conceptual Issue

Tax revenue in Nigeria is the income collected by various government levels through legally sanctioned taxes. Etim, Umoffon, and Ekanem (2020) describe tax revenue as a fiscal charge on individuals and corporations to fund public spending on goods, services, and social development. Similarly, studies by Ogbonna and Appah (2016) and Odoemelam (2018) defined tax as a levy imposed to fund government expenses. In Nigeria, the constitution specifies the taxes that can be collected by the different levels of government; these are the federal government, the state governments, and the local governments (Olaoye & Aguguom, 2018). Personal income tax, corporate income tax, value-added tax, and petroleum profit tax collected by the federal government of Nigeria were used in this study as measures of tax revenue.

The portion of the workforce in Nigeria that is gainfully employed is referred to as the employment level. The OECD (2024) describes the employment level as the ratio of employed people to the working-age population, which also indicates how well available labour is being engaged. The employment level is a crucial measure of a country's social stability, income distribution, and economic success. While low employment levels can be a sign of economic difficulties such as recessions, labour market problems, or high unemployment rates, a high employment level signifies a strong economy with job opportunities, capable of increasing income levels, improving living standards, reducing poverty, and fostering economic progress (Blanchard & Sheen, 2013). Furthermore, the employment level can influence government revenue and financial stability, as a highly employed labor force can help produce increased tax revenues for the government, leading to a sustainable financial environment (OECD, 2019). Largely, a growing economy creates more job opportunities and demand for labor. Hence, economic growth primarily causes a high employment level in a country.

2.2. Theoretical Review

John Maynard Keynes developed the Keynesian theory of fiscal policy in the 1930s, which serves as the foundation for this investigation. Keynesian economics places a strong emphasis on the role that taxes and public spending play in keeping the economy stable, particularly during recessions (Keynes, 1964). The multiplier effect, a fundamental tenet of the theory, states that as initial government investment stimulates further economic activity, higher government spending results in a greater than proportionate increase in national income and output. Tax policy has been greatly impacted by Keynesian theory, which promotes changes that raise government revenue to pay for infrastructure, public amenities, and job creation, all of which raise employment levels. Proponents contend that well-designed tax reforms encourage economic growth, lessen inequality, and redistribute income (Stiglitz, 2010). In contrast, critics argued that excessive government involvement can result in inflation, high debt, and inefficiencies. Notwithstanding, Keynesian theory provides insight into how tax reforms may influence economic growth, especially in emerging economies such as Nigeria. Studies by Ekong, Orebiyi, and Iriabije (2024) showed mixed results, suggesting that government spending and inclusive growth have long-term, favorable, but occasionally negligible relationships. Nonetheless, research by Dikeogu and Karma (2018) showed that macroeconomic performance and fiscal policy are related over the long term. These findings were corroborated by Cookey and Okorie (2020), which examined the relationship between fiscal policy tools and economic growth in the Nigerian economy.

2.3. Empirical Review

Studies on the relationship between tax revenue and employment levels in Nigeria have yielded varied results, in addition to being scanty. Balasoiu et al. (2023) found that corporate and personal income taxes negatively impacted economic growth in EU countries, while Souillard (2022) found employment growth in multinational companies that enjoy tax havens. Similarly, Domguia et al. (2022) found a positive influence of environmental taxes on employment in a sample of the OECD and non-OECD countries.

In Nigeria, George-Anokwuru (2022) showed that government expenditure had a positive but insignificant effect on employment, while the impacts of total tax revenue and external debt service were negative and significant. Similarly, Anichebe (2019) showed that tax policy affects unemployment in Nigeria, with company and personal income taxes reducing unemployment, while VAT increases unemployment. A prior study by Deskar-Škrbić, Drezgić, and Šimović (2018) revealed that tax policy significantly affects employment in Croatia and thus emphasises the necessity for tax reforms to balance revenue with employment spurs. Similarly, Zirgulis and Šarapovas (2017) examined the effect of corporate tax on unemployment in a sample of 41 countries. The study found that a rise in corporate tax rates increases unemployment levels. In a related study, Lora and Fajardo (2012) found that types of tax affect employment and labour market situation differently.

The available literature also shows that some previous studies focused mainly on the relationship between tax revenue and other aspects of economic performance, such as human capital, growth, and the labour market. Osirim et al. (2022) reported a statistically insignificant positive link between direct taxes and human capital development, except for company income tax. Similarly, Ofoegbu et al. (2016) found a positive relationship between tax revenue and economic development in Nigeria, and Abd Hakim (2020) showed that direct taxes negatively affect growth, while indirect taxes have a positive but insignificant effect on development. Similarly, Emeneka (2021) reported an adverse impact of personal income tax on GDP per capita in Nigeria.

This finding contradicts Obaretin and Uwaifo (2020), which showed that value-added tax (VAT) enhanced economic development in Nigeria. On the other hand, Gurdal, Aydin, and Inal (2021) established bidirectional causality between tax revenue and economic growth in the Group of Seven (G7) countries, while Lou, Zhang, and Wang (2019) linked high personal income tax rates in the U.S. to deterred skilled labor mobility, affecting economic growth and social welfare. These studies underscore the nuanced relationship between taxation, employment levels, and economic performance.

3. METHODOLOGY

To achieve the objective of this study, an ex-post facto research design was employed, utilizing time series data covering 43 years from 1980 to 2023. Ex-post facto time series data was used because the study examined the past event relationship between the dependent variable (employment levels) and the independent variables (tax revenue, measured by PIT, CIT, VAT, PPT). The period was chosen to ensure that patterns over time regarding the impact of tax revenue on employment levels in Nigeria were identified. Additionally, the extended period helped eliminate any effects of short-term fluctuations on the dynamics of tax revenue and employment levels in Nigeria. Data for the study were sourced from the Central Bank of Nigeria (CBN), the World Bank, and the Federal Inland Revenue Service (FIRS). The validity and reliability of the data were based on the fact that data from these sources are widely accepted in Nigeria and relied upon by stakeholders. The work of Anichebe (2019) was adapted and specified in its linear logarithmic format. Pre-estimation diagnostics showed that the time series data set of the variables exhibited a mixed order of integration *I(0)* and *I(1)*, with the existence of a long-run relationship between tax revenue and employment levels. These findings justified the use of the long-run Autoregressive Distributed Lag (ARDL) model as the appropriate analytical approach for the study. Consequently, the ARDL was specified as follows:

$$\Delta EMPR_t = a_0 + \sum_{i=1}^{N} a_1 \Delta EMPR_{t-1} + \sum_{i=1}^{N} a_2 \Delta LPIT_{t-1} + \sum_{i=1}^{N} a_3 \Delta LCIT_{t-1} + \sum_{i=1}^{N} a_4 \Delta LVAT_{t-1} + \sum_{i=1}^{N} a_5 \Delta LPPT_{t-1}$$
$$+ \omega_1 EMPR_{t-1} + \omega_2 LPIT_{t-1} + \omega_3 LCIT_{t-1} + \omega_4 LVAT_{t-1} + \omega_5 LPPT_{t-1} + \upsilon_t$$

Where:

EMPR represents Employment rate; PIT depicts Personal income tax; CIT denotes Company income tax; VAT is Value-added tax; PPT denotes Petroleum profit tax; t – regular time interval at which the values of variables were considered; ϵt = Error term, it accommodates the influence of other variables that determined EMPR but not directly included in the model; α_0 is the intercept or constant term; α_{1-5} are the parameters to be estimated; Δ is the first difference of operator.

Employment rate for the study, which represents the total number of people employed in both the formal and informal sectors and is expressed as a percentage of the population, was sourced from the World Bank records for 2023. The tax revenue measures of PIT, CIT, VAT, and PPT were sourced from the records of the CBN and the FIRS for 2023.

Table 1 Presents Descriptive statistics.

Table 1. Descriptive statistics.

Variable	Mean	Maximum	Minimum	Std. dev.
EMPR (%)	56.564	58.296	50.400	2.078
CIT (Billion Naira)	3,398,242.	33,480,000	403.000	7,575,703.
PIT (Billion Naira)	63.508	254.190	0.000	65.260
VAT (Billion Naira)	218.103	1,555.270	0.000	341.047
PPT (Billion Naira)	1,001,714.	4,209,000.	3,746.900	1,131,785.

4. RESULTS AND DISCUSSION

The descriptive statistics provide insights into the distribution and characteristics of the key variables. The EMPR has a mean of 56.56%, with a small range of variation between 50.40% and 58.30% and a standard deviation of 2.08%, indicating relative stability. CIT exhibits high variability, with a mean of 3.39 trillion Naira and a maximum of 33.48 trillion Naira, reflecting significant skewness and a non-normal distribution. Similarly, PIT shows fluctuations, with a mean of 63.51 billion Naira and a standard deviation of 65.26 billion Naira, as well as instances of zero recorded revenue. VAT revenue also demonstrates high volatility, with a mean of 218.10 billion Naira and a standard deviation of 341.05 billion Naira, confirming its non-normal distribution. PPT, with an average revenue of

1.00 trillion Naira and a maximum of 4.21 trillion Naira, exhibits considerable variation, though it deviates only slightly from normality. Overall, the tax revenue variables display significant fluctuations, suggesting underlying economic and policy influences affecting their distribution.

Table 2 presents a Partial Correlation matrix and the variance inflation factors.

Table 2. Correlation matrix and the variance inflation factors.

Variable	LOGCIT	LOGPIT	LOGPPT	LOGVAT	VIF
LOGCIT	1				1.091
LOGPIT	0.048	1			1.002
LOGPPT	-0.247	-0.014	1		1.133
LOGVAT	-0.194	0.001	0.238	1	1.103
Mean of variance inflation factor					1.082

The correlation matrix reveals weak relationships among tax revenue variables, with a negative correlation between LOGCIT and LOGVAT (-0.1945) and a low correlation between LOGVAT and LOGPPT (0.2383), indicating limited interdependence. Since no correlation exceeds 0.90, severe multicollinearity is not a concern (Gujarati & Porter, 2009). Variance Inflation Factor (VIF) values further align with this, as none exceed the critical threshold of 10, with LOGVAT having the highest VIF of 1.1031 and a mean VIF of 1.0822, suggesting no significant multicollinearity issues. These findings indicate that tax revenue variables are relatively independent, minimizing potential distortion in regression analysis.

Table 3. Unit root test.

Variable	Phillips–Perron unit root test			Integration
	Level	First diff.	Critical	
EMPR	-3.062	-	-2.931	I (0)
LOGCIT	-0.343	-8.607	-2.931	I (1)
LOGPPT	-0.909	-6.689	-2.931	I (1)
LOGVAT	-2.609	-4.303	-2.931	I (1)
LOGPIT	0.017	-8.627	-2.931	I (1)

The Philip-Perron (PP) unit root test was conducted to determine the stationarity of the variables used in the study. The results in Table 3 indicate that only EMPR was stationary at the level, with a PP test statistic of -3.0621, against the critical value of -2.9314. This implies that employment rate data does not exhibit a unit root and remains stable over time without requiring transformation. Conversely, the tax revenue variables (LOGCIT, LOGPPT, LOGVAT, and LOGPIT) were found to be non-stationary at the level, as their test statistics were greater than the critical value, indicating the presence of a unit root. However, after first differencing, all these variables became stationary, as their test statistics turned more negative than -2.9314.

Table 4. Bound test cointegration of tax revenue and employment level in Nigeria.

F-bounds test		Null hypothesis: No levels relationship		
Test statistic	Value	Significance	I(0)	I(1)
F-statistic	4.162*	10%	2.200	3.090
K	4	5%	2.560	3.490
		2.5%	2.880	3.870
		1%	3.290	4.370

Note: "*" Indicates significance.

The cointegration test of bounds was presented in Table 4 to assess whether a long-run relationship exists among the variables. The F-statistic shows a value of 4.162, which is higher than the upper bound value of 3.49 at the 5%

significance level. This confirms the existence of a long-run relationship between tax revenue and employment level in Nigeria.

Table 5 presents Estimation outcomes.

Table 5. Estimation outcomes.

Short-run estimates				
Dependent variable: EMPR				
Variable	**Coefficient**	**Std. error**	**t-statistic**	**Prob.**
D(EMPR(-1))	0.262	0.133	1.972	0.067
D(EMPR(-2))	-0.494	0.136	-3.626	0.003
D(LOGPIT)	0.232	0.380	0.611	0.550
D(LOGCIT(-1))	0.334	0.095	3.536,408	0.003
D(LOGVAT)	0.683	0.586	1.165	0.262
D(LOGVAT(-1))	2.975	0.695	4.278	0.001
ECT(-1)	-0.267	0.046	-5.770	0.000
Long run estimates (*ARDL*)				
LOGPIT	13.585	2.605	5.214	0.007
LOGCIT	-3.951	0.658	-6.000	0.004
LOGVAT	-3.384	0.891	-3.797	0.019
LOGPPT	3.078	0.639	4.816	0.009
C	27.804	8.081	3.441	0.026
Evaluation tests				
		Statistics	Prob.	
R-squared		0.746	-	
Adjusted R-squared		0.657	-	
F-statistic		17.828	0.000	
Post estimation diagnostic results				
Diagnostics		Chi-square	Prob.	
Serial correlation LM test		0.285	0.756	
Heteroskedasticity test:		1.371	0.278	
Normality test		0.385	0.825	

The short-run estimates show that the error correction term (ECT(-1)) is negative (-0.2673, p = 0.0000), confirming the stable long-run relationship between tax revenue and employment, with about 26.7% of disequilibrium corrected each period. The lagged employment variable D(EMPR(-1)) has a positive coefficient (0.2617, p = 0.0673), indicating some persistence in employment trends, although it is not statistically significant at the 5% level. However, the second lag of employment D(EMPR(-2)) is negative (-0.4942, p = 0.0025), suggesting that past employment levels have a significant inverse impact on current employment, possibly due to structural adjustments in the labor market or delayed policy effects. Regarding tax components, current Company Income Tax (D(LOGCIT)) positively influences employment (0.4331, p = 0.0022), meaning that short-term increases in corporate tax revenue support job creation. The lagged CIT variable (D(LOGCIT(-1))) also remains positive (0.3344, p = 0.0030), reinforcing the notion that corporate tax revenue contributes to employment over time. Additionally, lagged VAT (D(LOGVAT(-1))) has a strong positive impact (2.9748, p = 0.0007), implying that indirect tax revenue from consumption tax plays a delayed but significant role in employment generation. These findings are consistent with some recent previous studies (Balasoiu et al., 2023; George-Anokwuru, 2022; Kujore, Dada, & Adegbie, 2021).

However, the long-run estimates indicate that CIT (LOGCIT) and VAT (LOGVAT) negatively impact employment, with coefficients of -3.9508 (p = 0.0039) and -3.3839 (p = 0.0191), respectively. This suggests that as corporate and consumption taxes increase, employment levels tend to decline. On the other hand, PIT (LOGPIT) and PPT (LOGPPT) have significant positive effects on employment, with coefficients of 13.585 (p = 0.007) and 3.078 (p = 0.009), respectively. This implies that increased revenue from these tax sources supports employment growth. The constant term (C) is 27.8037 (p = 0.0263), indicating that even in the absence of changes in tax revenue, baseline

employment remains positive. These findings lend credence to the studies by Emeneka (2021) and Gurdal et al. (2021) but contradict the findings by Domguia et al. (2022).

The adjusted R-squared (0.6575) indicates a good model fit, showing that tax revenue variables explain a substantial portion of 65.75% of the variation in employment levels in Nigeria. The F-statistic value of 17.828, with a probability value of 0.000, indicates that the model is statistically significant at the 5% level. Hence, the study rejects the null hypothesis of no significant effect of tax revenue on employment levels and concludes that tax revenue significantly affects employment levels in Nigeria.

The Serial Correlation LM Test (Chi-Square = 0.2852, p = 0.7564) shows no evidence of autocorrelation, suggesting that the residuals are not correlated over time. The Heteroskedasticity Test (Chi-Square = 1.3707, p = 0.2784) confirms that the variance of the error terms is constant, indicating no heteroskedasticity issues. The Normality Test (Chi-Square = 0.3849, p = 0.8249) suggests that the residuals follow a normal distribution, which supports the reliability of statistical inferences drawn from the model. Furthermore, both CUSUM and CUSUMSQ stability tests confirm that the estimated model remains stable over time. The post-test diagnostics confirm that the results have no major econometric issues.

Figure 1 illustrates CUSUM squares for tax revenue and employment level in Nigeria.

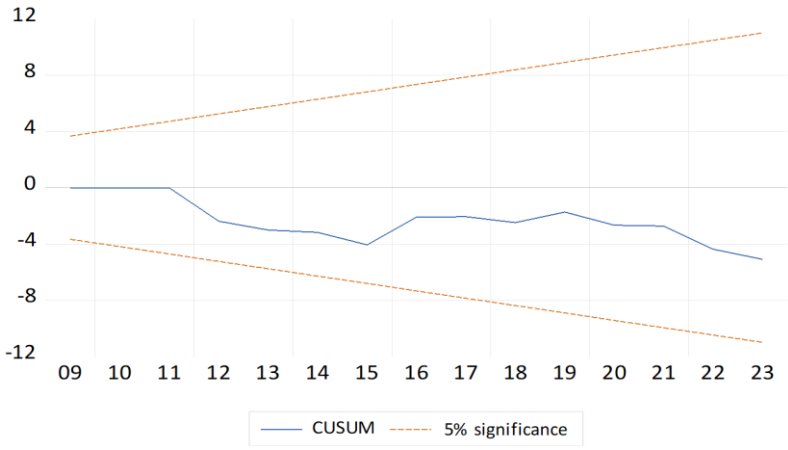

Figure 1. CUSUM squares for tax revenue and employment level in Nigeria.

Figure 2 illustrates the CUSUM test for tax revenue and employment levels in Nigeria.

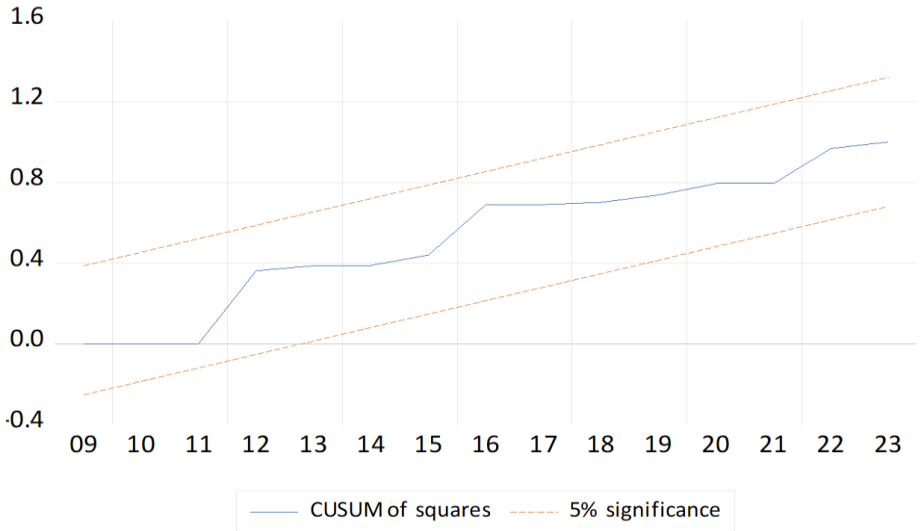

Figure 2. CUSUM test for tax revenue and employment level in Nigeria.

5. CONCLUSION AND RECOMMENDATIONS

The findings showed that the impacts of company income tax and value-added tax on employment levels were positive and significant in the short run, while the impact of personal income tax was positive but insignificant. On the other hand, the long-run impacts of personal income tax and petroleum profit tax on employment levels were positive and significant, while the impacts of company income tax and value-added tax were negative and significant. Therefore, the study concludes that tax revenue has heterogeneous impacts on employment levels in Nigeria, which results from the different tax components. Accordingly, the study recommends reforming the country's tax structure to support economic performance initiatives, as these will promote growth in employment levels. In addition, given that the tax revenue sources did not exhibit a constant effect on the test variable, the study recommends a review of existing tax-based project funding arrangements to ensure efficacy in the allocation and utilization of funds for planned purposes. Furthermore, the study recommends a comprehensive analysis by policymakers of the economic environment concerning how economic performance indicators, such as employment levels, react to changes in the tax ecosystem before implementing future tax policy changes.

Accordingly, the study recommends reforming the country's tax structure to support economic performance initiatives, as these will cause growth in employment levels. In addition, given that the tax revenue sources did not exhibit a constant effect on the test variable, the study recommends a review of existing tax-based project funding arrangements to ensure efficacy in the allocation and utilization of funds for planned purposes. Furthermore, the study recommends a comprehensive study by policymakers of the economic environment concerning how economic performance indicators, such as employment levels, react to changes in the tax ecosystem, before future tax policy changes.

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