PDF - THE IMPACT OF TAX INCENTIVES ON INDUSTRIAL SECTOR DEVELOPMENT IN NIGERIA - researchcub.info**ABSTRACT**

This research studied the impact of tax incentives on industrial sector development in Nigeria from 1981 to 2009 using time series data. The Ordinary Least Square (OLS) method was adopted using a Classical Linear Regression Model and the E-View version 6.0 software. Two models were used to determine the impact of subsidies, government expenditure and exports on both industrial output and investment respectively. The result showed that subsidies and government expenditure have significant impacts on industrial output and investment and thus have a great potential to boost industrial output, promote investment, and bring about industrial sector development in Nigeria. Overall, the result suggests that tax incentives have a significant impact on industrial sector development in Nigeria.

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CHAPTER ONE

INTRODUCTION

BACKGROUND OF THE STUDY

The industrial sector remains a strong and vibrant sector of the economy and an integral part of development, structural change and self-sufficiency; playing a vital role in the economic growth and development of any given nation. The development of the industrial sector would therefore, also mean or translate into the development of the economy. Thus, resources have been channeled into this sector through heavy public sector investment, especially import – substitution basic industries, through general financial incentives and tax incentives in addition to a high level of protection for private investment.

According to Anyanwu (1993), the industrial sector is made up of four sub-sectors viz: manufacturing, processing, craft and mining sub sectors. The manufacturing sub-sector is involved in the conversion of raw materials into finished consumer goods or intermediate or producer goods. The processing sub-sector is involved in the treatment of raw materials or food for preservation or conversion into consumable commodities. The craft sector carries out activities involving a special skill at making things, especially with the hands or simple tools. And mining sub-sector carries out activities of mining, exploration of mineral or natural resources like crude oil, etc.

The socio-economic environment of Nigeria has been most devastating for the industrial sector, especially the manufacturing sub-sector. As at last count, more than 850 manufacturing companies have had to close shop in a short space of time due to problems in the country's operating environment. In 2009, 37 of such companies stopped operations, undermining utilization and the contribution of the manufacturing sector to the country's GDP.

The problem assailing the operation of the sector include chronic lack of infrastructure, multiple and excessive taxation as the government continues with the relentless drive to increase internally generated revenue; exorbitant costs of raw materials, delay due to bureaucracy at the ports as goods are cleared, lack of adequate security among others.

In Nigeria, taxation is used as a major fiscal policy tool for the attainment of macroeconomic objectives and to influence the working of the economic system in order to achieve specific economic goals and the desired level of investment needed for economic growth and development. It is also a primary source of government revenue in Nigeria besides oil. However, taxation has posed a lot of problems to the development of the industrial sector. When the government taxes earnings from investment, it becomes a problem for firms to raise adequate resources in the capital market. When retained profits are taxed, firms fail to depend on their internal resources for expansion, but resort to borrowing if they can obtain such loans. Thus, the total capacity to invest is likely to decrease.

In pursuit of the achievement of economic goals set, government introduces a number of incentives in the annual budget. These incentives are designed to encourage investments in certain preferred sectors of the economy, and which are sometimes geared towards attracting inflow of foreign exchange to complement domestic supplies for rapid development. Tax concessions have therefore been given to pioneer or newly established industries for a number of years, in the form of tax exemption, reduction of tax rate, reduction of import duty on imported raw materials, among others. All these measures have been adopted by the government to reduce production costs (subsidize production) and encourage the establishment and expansion of industries in Nigeria.

Justifiable concern has however been often expressed by developing countries over the potential effect of their incentive schemes. Some have openly acknowledged their inability to attract the desired level or quality of investment, in spite of the generosity of their incentive programmes. One basic fact is that industries are likely to produce a limited response no matter how lavish they are, if the general investment climate is not favourable. “No amount of incentives would for instance, compensate for a small internal market, a stagnant economy or political instability”. (Okafor, 1983).

The industrial sector still faces a lot of difficulties which hamper its development. Firms are not encouraged to invest and are not interested in investing in projects with long gestation periods, and the level of tax evasion, avoidance and capital flight is still on the rise. It is against this background that the research is undertaken, to study the impact of tax incentives on industrial sector development in Nigeria.

1.2 STATEMENT OF RESEARCH PROBLEM

Nigeria in its quest to develop the industrial sector encounters some bottlenecks or factors that militate against such attempts. For the purpose of this research, it is necessary to study such problems and proffer solution to such problems.

A major problem facing the industrial sector thereby impeding its development is the problem of excessive taxation in the form of high tax rate, double and multiple taxation. Although taxation forms one of the major sources of revenue to government apart from oil, it affects firms negatively. Thus higher tax rates serve as disincentive to firms for investment and expansion as it leaves firms with less money to reinvest thereby discouraging productivity and investment and a decrease in the level of output by the industrial sector.

Another problem that hampers the growth and development of the industrial sector in Nigeria is the problem of low price elasticity of exports and lack of comparative advantage. This means that Nigeria’s foreign market share cannot appreciate despite the incentives granted the industrial sector.

Non-availability of data was a major research problem as there is currently no data on tax incentives in Nigeria.

TABLE 1: INDUSTRIAL OUTPUT AND INVESTMENT IN NIGERIA

YEAR	INDUSTRIAL OUTPUT	INDUSTRIAL OUTPUT GROWTH	INVESTMENT	INVESTMENT GROWTH
1981	15802.6		18220.6	
1982	14424.7	-1377.9	17145.8	-1074.8
1983	13596.8	-827.9	13335.3	-3820.5
1984	14470.8	874	9149.8	-4185.5
1985	18226.4	3755.6	8799.5	-350.3
1986	16392.9	-1833.5	11351.5	2552
1987	34477.3	18084.4	15228.6	3877.1
1988	41200.3	6723	17562.2	2273.6
1989	89596.7	48396.4	26825.5	2333.6

1990	115591.4	25994.7	40121.3	13295.8

SOURCE: CBN Statistical Bulletin 2009

From the above table, it can be observed that the level of investment declined between 1981 and industrial output also recorded negative values (decline). But from 1985 and 1986 industrial output and investment respectively began to record positive growth.

From the foregoing, the following questions are relevant to guide the research:

What are the impacts of tax incentives on industrial output in Nigeria?

What are the impacts of tax incentives on investment in Nigeria?

1.3 OBJECTIVES OF THE STUDY

For the purpose of this study, industrial output and investment are adopted as measures of industrial sector growth. The broad objective is to determine the impact of tax incentives on industrial sector development in Nigeria.

The specific objectives are:

To determine the impact of tax incentives on industrial output in Nigeria.

To determine the impact of tax incentives on investment in Nigeria.

RESEARCH HYPOTHESIS

The research is guided by the following hypotheses:

H_0: Tax incentives have no significant impact on industrial output in Nigeria.

H_0: Tax incentives have no significant impact on investment in Nigeria.

1.5 SIGNIFICANCE OF THE STUDY

The research will be of benefit to the government – policy makers and tax revenue authorities. It will provide a framework for the critical evaluation of tax policies, provides a basis for the modification of tax incentive design and identify loopholes in the present tax system that serves as disincentive to investment.

It will also benefit other researchers, forming a basis for further research on the subject in future.

1.6 SCOPE AND LIMITATION OF THE STUDY

The research covers a period of 29 years from 1981 to 2009

The limitation of the study includes non-availability of related or necessary data for the research.

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