“Internally generated revenue and capital expenditure of the public sector in the southwestern states of Nigeria”

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INTERNALLY GENERATED REVENUE AND CAPITAL EXPENDITURE OF THE PUBLIC SECTOR IN THE SOUTHWESTERN STATES OF NIGERIA

Abstract

The paper examines the effect of internally generated revenue (IGR) on the capital expenditure of the southwestern states in Nigeria. Tax, fines, and fees, as well as earnings and sales, are used to measure the revenue generated through internally generated revenue (IGR), while the amount spent on the provision of capital assets like roads, building construction, and other social amenities is used to measure capital expenditure incurred during the period under review. Secondary data were collected from each of the six southwestern states of Nigeria's Internal Revenue Service Boards, the Office of the Accountant General of each of the six Southwestern States, the Central Bank of Nigeria (CBN), and the National Bureau of Statistics (NBS) over 1999–2023. Descriptive statistics, correlation analysis, and multiple regression methods with other diagnostic tests, such as the unit root test and heteroskedasticity, were conducted. Findings showed that both taxes and earnings and sales have a positive and significant effect on capital expenditure in southwest Nigeria. In comparison, fees and fines have a negative and significant influence on capital expenditure. The study concluded that there is a significant relationship between internally generated revenue (IGR) and the development of capital expenditure in the southwestern states of Nigeria. It is recommended that the government focus on strategies to increase revenue through IGR.

Keywords capital expenditure, earnings and sales, fines and fees, internally generated revenue, taxpayer

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INTRODUCTION

The importance of internally generated revenue (IGR) as a crucial factor of infrastructure development in Nigeria is becoming more recognized by policymakers and experts. Despite widespread recognition of IGR's role in funding capital projects, there remains a lack of understanding about how different IGR components, such as taxes, fines, and fees, contribute to long-term infrastructural investment, particularly in Nigeria's southwestern states (Ajaero et al., 2024). Articles primarily focus on cross-sectional analyses or short-term relationships, which fail to capture the dynamic patterns and causal factors driving infrastructure development (Abdulrahman et al., 2024).

This gap is critical because effective revenue generation is essential for reducing dependency on federal allocations and external debt, promoting financially independent growth, particularly during the post-pandemic economic recovery (Dzigbede et al., 2023). Furthermore, the shortage of comprehensive studies on IGR components restricts the development of targeted policies that aim to increase revenue re-

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sources for long-term infrastructure investment. Addressing this gap is crucial for advancing empirical understanding, as it offers valuable insights into how regional governments can optimize revenue streams to foster infrastructure development.

1. LITERATURE REVIEW

Apalowowa et al. (2025) described revenue as the aggregate sum of money collected by a government from all sources within a specific timeframe. Abdulwahab and David (2023) echoed this sentiment by defining revenue as the overall earnings an organization makes to support its operations. Government revenue originates from various channels, including licenses, fees, proceeds from the sale of government assets, tax revenues, and penalties. Additional revenue streams may include income derived from loan issuance, investment sales, agency or private trust transactions, and intra-governmental transfers. Consequently, revenue constitutes the comprehensive income accrued to the state governments from various channels, encompassing IGR, statutory allocations from the federal government, and other avenues. A considerable portion of the total revenue for states and local governments is generated internally.

Internally generated revenue (IGR) signifies a government's capacity to finance its development projects and administrative expenses without reliance on external or federal funding, thereby illustrating fiscal independence and effectiveness (Adegboyo et al., 2021). Critics argue that improving IGR is essential for achieving financial independence; however, it should be balanced with fair taxation and accountability to prevent social unrest and economic distortions. IGR is intrinsically linked to fiscal decentralization and governance quality. The effective management of IGR enhances a region's capacity to finance local projects, deliver public services, and reduce dependence on central government transfers (Abdulwahab & David, 2023). Internally generated revenue is a crucial financial metric for sub-national governments and public sector entities, representing income derived from internal sources such as taxes, fees, fines, and diverse revenue-generating activities (Ajaero et al., 2024). Thus, the IGR is classified under the foregoing subheading taxes, which serve as crucial fiscal policy tools used by governments to generate revenue, influence economic decisions, and promote public goods and services (Adebayo & Olatunji, 2023). Tax is described as a compulsory financial obligation imposed by a governing authority on individuals or corporations to fund governmental expenditures without a direct provision of services (Iyidiobi et al., 2022).

Fines and fees are important components of a nation's revenue-generating mechanisms and regulatory enforcement strategies. Conceptually, fines are sanctions imposed for violations of laws or regulations, serving as punitive measures to deter misconduct and ensure compliance (Agama & Onowu, 2025). Fees represent charges imposed for services or permits offered by government agencies, serving mainly as mechanisms for cost recovery rather than as punitive actions (Akinwumi & Oladipo, 2024). Fines and fees serve as sources of government revenue, yet their intended purposes are markedly distinct.

Fines act as dual mechanisms of deterrence and punishment, generally associated with legal transgressions, including traffic infractions and environmental violations (Akintola et al., 2024). Such measures are typically reactive, implemented following violations. Fees are structured to be anticipatory and centered on the delivery of services, linked to licensing, permits, or administrative costs, and aim to recover expenses related to the provision of services (Okafor & Onugu, 2025).

Earnings and sales in the public sector are distinct analytical functions for assessing government financial performance. Gross revenue or total IGR captures the top-line government revenue base and is essential for evaluating revenue capacity, economic activity, and the effectiveness of revenue administration (Adekoya et al., 2023). It is frequently used to assess fiscal effort and revenue autonomy.

Capital expenditure (CAPEX) denotes governmental financial outlays directed toward the acquisition, construction, or improvement of long-term assets, including educational institutions,

healthcare facilities, transportation networks, and various public infrastructure projects. The aim is to foster economic growth, enhance quality of life, and support the public through investments in initiatives that will generate future returns (Ajiteru et al., 2018). Capital expenditure investments often promote economic growth and provide environmental advantages. Recurrent expenditures denote the financial resources required for a company's continuous operations, while capital expenditures relate to investments in long-term infrastructure improvements and economic stability (Ajaero et al., 2024).

Expenditure is essential for addressing infrastructure issues and enhancing resource allocation. Development expenditure includes both capital and ongoing costs aimed at enhancing economic and social conditions, whereas capital expenditure specifically pertains to funds designated for long-term infrastructure projects (Okiakpe et al., 2024). Development expenditure encompasses a broader array of expenses, including social services, while capital investment pertains exclusively to material assets. Corruption, inadequate project management, and insufficient transparency are critical considerations in capital expenditure planning, as these elements can result in inefficiency or misallocation (Ogbonna et al., 2024). Excessive dependence on capital projects, lacking sufficient planning, may obstruct debt repayment and negatively impact the economy (Njoku et al., 2024). Effective management of capital investments can enhance infrastructure and drive substantial economic development.

Capital expenditures are essential for infrastructure development and the sustained stability of the economy. Recent research highlights its significance; however, considerable challenges persist in resource allocation, project management, and governance. Optimizing capital expenditures necessitates a comprehensive approach encompassing capacity development, transparency, and strategic planning.

This study is underpinned by resource mobilization theory developed by Becker (1963) and other scholars examining elite and society movements. The concept posits that a government or local authority's capacity to generate revenue independently is contingent upon its efficacy in using resources under its jurisdiction. This encompasses efficient revenue collection, broadening the tax base, and enhancing administrative efficacy. This concept underscores the need to enhance administrative capacity and expand the tax base to increase internally generated revenue (IGR). It enhances economic autonomy, reduces dependence on external assistance or federal funding, and promotes sustainable development locally by emphasizing the efficient use of resources and company operations. A significant issue is its inability to account for structural challenges, such as inadequate institutional frameworks, economic disparities, or informal sectors, which complicate capital acquisition. Excessive emphasis on resource acquisition may result in elevated taxation, adversely affecting taxpayers and hindering economic advancement if mismanaged. This theory is crucial since the study examines the impact of internal revenue generation on capital expenditure and growth within Nigeria's governmental sectors. Comprehending the effective collection of resources would enable the state government to enhance IGR, which is crucial for sustainable development and reducing reliance on external financing (Adebayo & Olatunji, 2023).

Ajike et al. (2020) investigated the impact of internally generated revenue on infrastructural development in Lagos State, Nigeria (1998–2018). The study employed an ex-post facto research design and annual time-series data over a twenty-one-year period. The findings showed that internally generated revenue components had a significant effect on transport infrastructure in Lagos State, Nigeria. The study therefore recommended that the state government should utilize internally generated revenue for the development of transport infrastructure, to bring an improved standard of living, increase gross domestic product, and boost economic growth.

In Bauchi State, Nigeria, Hammayo et al. (2020) examined how state government funding affected the growth of the state's infrastructure. Secondary data were obtained from the government's annual financial statements covering the years 2006 through 2018. The ordinary least squares regression analysis method was used. The results showed that the federation account was favorable, but

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other receipts, including contributions from local governments for the implementation of cooperative projects, as well as grants and support from domestic and international sources, revealed a negligible link.

Furthermore, Okon and Uwah (2023) assessed the relationship between internally generated revenue and infrastructural development, as measured by capital expenditure, in Akwa Ibom State for the period 2007–2020. The objective was to ascertain the contribution of internally generated revenue to infrastructural development in health, education, and sanitation. Secondary data were obtained from the office of the Accountant General of Akwa Ibom State. The data were analyzed using simple regression analyses to test the hypotheses. It was discovered that internally generated revenue (IGR) has a positive relationship with infrastructural development in the state, which shows a positive and significant relationship with development in education, and an insignificant but positive relationship with health and sanitation.

Sokoh (2023) examined the internally generated revenue (IGR) in Delta State as a tool for infrastructural development. Ordinary least squares was applied to the secondary data obtained from 2008 to 2018. The results indicate that internally generated revenue has an insignificant impact on government health expenditure, whereas internally generated revenue by the Delta State Government has a significant effect on government expenditure on education infrastructure.

Moreover, Okereke and Olewe (2023) investigated how internally generated revenue affects the provision of road infrastructure, educational development, and water supply by Enugu State Local Government Authorities. Chi-square statistical analysis and mean score were used to analyze the data. They found that while internally generated cash had little impact on the provision of water infrastructure, it had a significant effect on the provision of road and educational infrastructure.

The relationship between internally generated revenue (IGR) and infrastructural development has been examined in several studies. For instance, Nkechi and Onuora (2018) investigated this relationship among the five southeastern states. Orisanaiye et al. (2020) and Ajiteru et al. (2018) examined the impact of tax revenue on infrastructural development in Osun State; however, their studies did not use secondary data and were limited in scope. Moreover, Olabisi et al. (2020) examined the relationship between IGR and capital development in Lagos Metropolis. These prior studies are different from this study in that all components of IGR are examined, and wider samples of state governments in the western geopolitical zone of Nigeria are taken.

Prior studies produced varied and sometimes contradictory findings. Some identified a positive but minor correlation between IGR and infrastructural development, while others reported a negative yet significant relationship. This study sets itself apart by examining internally generated revenue and capital expenditure in Western Nigeria, and dissecting IGR into three components, which are tax, fines and fees, and earnings and sales. Prior research on IGR and infrastructural development did not extend beyond 2022 and failed to depict the trend of capital expenditure in the southwestern states.

Therefore, this study aims to investigate the impact of internally generated revenue on the efficiency of capital expenditure in the southwestern states over 25 years, from 1999 to 2023.

2. METHODOLOGY

The population consists of Ekiti, Ondo, Ogun, Osun, Oyo, and Lagos States, which are the six states of Southwestern Nigeria, for the years 1999 to 2023. The states were selected based on the six geopolitical zones and the availability of relevant data. Secondary data were retrieved from each of the six Ministries of Finance of Southwestern States, each of the six South Western States of Nigeria Internal Revenue Service Board, and the Office of the Accountant General of each of the six South Western States, Central Bank of Nigeria (CBN), and National Bureau of Statistics (NBS). The information covered variables about the state's IGR, such as taxes, fees, and fines, earnings and sales, and capital expenditure (CAPEX) growth from 1999 to 2023. A summary of the variable measurements is presented in Table 1. The study

Table 1. Summary of variable measurement

Variables	Type of Variable	Description, Definition, and Type of Measures	Measurement/Justification
Capital Expenditure	Dependent Variable	LOG of CAPEX	Public sector capital expenditure (CAPEX) is measured as the total amount spent on acquiring, constructing, or improving long-term assets within a specified timeframe
Internally Generated Revenue	Independent Variables	LOG of IGR	Internally generated revenue (IGR) is measured by log of tax collected (LTAX), log of earnings and sales (LEAS), and log of fines and fees (LFAF)
		Log of Tax collected (LTAX)	Log of tax on income deducted directly from employees' wages and salaries, and indirect tax
		Log of Earnings and Sales (LEAS)	Log of rent from government-owned buildings, land, or other assets
		Log of Fines and Fees (LFAF)	Log of revenue collected from penalties for violations of the law

employed both descriptive and inferential statistical methods, multiple regression to analyze the data, in addition to relevant diagnostic tests.

This study investigated the correlation between IGR (proxies as taxes, fines, and fees – FAF), earnings and sales (EAS), and the capital expenditure (dependent variables) in Nigeria. The empirical model was adapted from Olaoye and Olugbamiye (2019). The model is specified in both functional and stochastic forms as follows

$$LCAPEX = f\left(LTAX,\ LFAF,\ LEAS\right). \quad (1)$$

This can be specified in operational form as:

$$LCAPEX_{it} = \beta_0 + \beta_1 LTAX_{it} + \beta_2 LFAF_{it} + \beta_3 LEAS_{it}\ \mu_{it}, \quad (2)$$

where *LCAPEX* = Log of Capital Expenditure; β_0 = Constant Coefficient; β_1 = Slope or regression parameters; *LTAX* = Log of Tax; *LFAF* = Log of Fines and Fees; *LEAS* = Log of Earnings and Sales; μ = Stochastic error term; *t* = Time series.

A priori expectation is that is $\beta_1 > 0$, $\beta_2 > 0$, $\beta_3 > 0$.

3. RESULTS AND DISCUSSION

The result of descriptive analysis in Table 2 shows that the medians of the variables are approximately 9.65 for IGR and 9.99 for CAPEX, both of which are lower than their means of 9.78 for IGR and 10.00 for CAPEX. This suggests that the data display positive skewness, with several high outliers raising the mean, even though most observations are concentrated around lower values. IGR and CAPEX exhibit maximum values of 12.15 and 11.99, respectively, while their minimum values are recorded at 6.65. The standard deviations of approximately 0.76 for IGR and 0.70 for CAPEX indicate significant variability in the data, as evidenced by the comparatively high maxima relative to the minima. The data indicate a notable level of variability in the observations. The distribution shape is confirmed by the positive, albeit modest, skewness values (0.218 for IGR and 0.302 for CAPEX), indicating a tendency for the data to display a more pronounced right tail. Kurtosis scores near 3 (2.895 for CAPEX and 2.895 for IGR) suggest distributions that are slightly peaked yet approximately normal. The variables exhibit deviations from a normal distribution, as indicated by the significant Jarque-Bera statistics (approximately 7.08 for IGR and 7.082 for CAPEX) with *p*-values below the standard 0.05 threshold. The distributions deviate from normality, as indicated by the significant outcomes of the Jarque-Bera test, which must be considered in subsequent analyses.

Table 3 shows the results of the unit root test for both IGR and CAPEX, which are integrated of order one (I(1), indicating they are non-stationary in their initial state but become stationary upon taking their first differences. The correlation matrix shows that the log of internally generated revenue (LIGR) and the log of capital expenditure (LCAPEX) are strongly correlated. The two variables have a correlation value of around 0.993. There is an almost perfect positive link between the growth of capital expenditure and gains in domestically produced revenue.

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Table 2. Descriptive analysis

Variables	Obs	Mean	Median	Max	Min	Std. Dev	Skewness	Kurtosis	Jarque Bera	Prob.
LCAPEX	150	10.004	9.996	11.998	8.791	0.703	0.30	2.895	7.082	0.029
LTAX	150	9.783	9.648	12.149	6.650	0.761	0.218	4.630	17.789	0.000
LFAF	150	9.579	9.504	11.950	8.0352	0.799	0.608	3.058	9.254	0.010
LEAS	150	9.4002	9.317	1.757	7.8859	0.801	0.570	3.003	8.123	0.017

Table 3. Unit root test

Variables	Levin, Lin & Chu t* Statistics	P-values	Order of integration	REMARK
LCAPEX	–2.36412	0.0000	1(1)	Stationary
LTAX	–6.48963	0.0000	1(1)	Stationary
LFAF	–3.73001	0.0001	1(1)	Stationary
LEAS	–4.79383	0.0000	1(1)	Stationary

Table 4 shows the analysis of the correlation matrix indicates robust positive relationships among the variables associated with internally generated revenue (IGR), and the development of capital expenditure. The correlation coefficients between the logarithm of tax administration variables, including Tax, Fine and Fees, and Earnings and Sales, and the logarithm of capital expenditure development are significantly elevated, often exceeding 0.84.

Table 4. Correlation matrix

Variables	LCAPEX	LTAX	LFAF	LEAS
LCAPEX	1	–	–	–
LTAX	0.842	1	–	–
LFAF	0.862	0.876	1	–
LEAS	0.869	0.877	0.998	1

According to the matrix in Table 5, the covariance between LCAPEX and LIGR is 0.254, indicating a positive degree of linear association; when internal revenue increases, capital expenditure tends to increase as well, though the strength of this relationship is moderate rather than strong. In contrast, the covariance values between other variables, including tax-related measures like LTAX, LFAF, and LEAS, and LCAPEX, are relatively low and, in some cases, negative (e.g., LTAX at –0.024 and LFAF at –0.116), suggesting weak or negligible relationships with capital expenditure. For example, the covariance between LTAX and LCAPEX being –0.024 indicates that variations in tax revenue are not substantially associated with fluctuations in capital expenditure in this dataset, and the marginal negative value hints at a very weak inverse relationship, but not a significant one. The Breusch-Pagan-Godfrey heteroskedasticity test determines whether a regression model's error variance is constant (homoskedasticity) or changes (heteroskedasticity). The results of the Breusch-Pagan-Godfrey test of this study show that the *p*-values are all greater than the significance level ($p<0.05$), indicating that there is heteroskedasticity present in the regression model used in the study.

Table 5. Coefficient covariance matrix

Variables	C	LTAX	LFAF	LEAS
LCAPEX	0.254	–0.024	–0.116	0.116
LTAX	–0.024	0.006	0.008	0.012
LFAF	–0.116	0.008	0.231	0.231
LEAS	0.116	0.012	0.231	0.236

Table 6 shows the results of the heteroskedasticity test for the explanatory variables in the model. The p-values for LTAX (0.0003), LFAF (0.0000), and LEAS (0.0000) are all statistically significant at the 5% level. This result leads to the rejection of the null hypothesis of homoskedasticity, indicating heteroskedasticity in the regression model.

Table 6. Heteroskedasticity test

Variables	P-value
LTAX	0.0003
LFAF	0.0000
LEAS	0.0000

The empirical results in Table 7 indicate that taxes have a positive and statistically significant influence on capital expenditure (Coeff = 0.199; $p < 0.05$). This implies that if taxes generate substantial revenue, the government can allocate more funds toward essential infrastructure projects, social services, and de-

Table 7. Regression results

Variables		Pooled	Fixed Effect	Random Effect
LTAX	Coefficient	0.320	1.168	0.199
	Standard Error	0.073	0.079	0.076
	T. Statistics	4.375	2.133	2.620
	Probability	0.000	0.035	0.0097
LFAF	Coefficient	–0.009	–1.782	–1.616
	Standard Error	0.496	0.481	0.472
	T. Statistics	–2.032	–3.666	–3.426
	Probability	0.0439	0.000	0.000
LEAS	Coefficient	1.499	2.314	2.159
	Standard Error	0.497	0.485	0.476
	T. Statistics	3.016	4.787	4.537
	Probability	0.003	0.000	0.000
Constant	Coefficient	2.439	3.486	3.242
	Standard Error	0.363	0.504	0.474
	T-Statistics	6.714	6.913	6.841
	Probability	0.000	0.000	0.000
Hausman	R-squared	0.789	0.841	0.733
	F-stat	181.877	92.885	133.288
	Durbin Watson	0.899	1.060	1.040
	Prob. (F-Stat)	0.000	0.000	0.000
	Probability	0.2770	–	–

velopment initiatives. This can lead to improved public facilities, better transportation networks, and enhanced community services, directly benefiting the local population. Fees and fines have a negative and significant influence on capital expenditure (Coeff = –1.616; $p < 0.05$). This suggests that an increase in reliance on these revenues may hinder the government's ability to invest effectively in public infrastructure and services. Earnings and sales have a positive and significant influence on capital expenditure (Coeff = 2.159; $p < 0.05$). This indicates that higher revenues from these sources can lead to increased investments in infrastructure and public services. When earnings, such as those from government-owned enterprises or activities, and sales revenues from goods and services are strong, the government has more financial resources to allocate towards capital projects. In the southwestern states of Nigeria, public sector capital expenditure increases alongside enhancements in internal revenue streams, as indicated by the random effects model, primarily driven by investments in IGR. Locally generated resources are essential for fostering development investment, evidenced by their statistical significance and considerable explanatory power.

The influence of internally generated revenue (IGR) on capital expenditure (CAPEX) is essential for understanding the significance of fiscal resources in infrastructure progress within Nigerian governments. Internally generated revenue (IGR), including taxes, fines, fees, and other sources, is crucial for financing public projects, especially when foreign aid and federal funds are insufficient or inconsistent (Adebayo & Olatunji, 2023). The effective mobilization and management of IGR directly affect the budgetary capacities of state governments to implement capital projects, such as roads, educational institutions, and healthcare facilities.

The study establishes a significant correlation between IGR and CAPEX, bolstered by strong statistical evidence, affirming that IGR is a vital predictor of infrastructure development in the region. A notable finding was the very high correlation coefficients (surpassing 0.97) seen between IGR variables and capital expenditure, perhaps suggesting multicollinearity issues within the model. This finding requires careful interpretation, since high correlations may amplify the perceived strength of the association, perhaps resulting in an overestimation of IGR's genuine impact on capital development.

Comparing this finding with previous research reveals both agreement and discrepancy. The results support Ogbonna's (2024) assertions, demonstrat-

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ing that increased revenue from internal sources is positively correlated with infrastructure investment in Nigeria. Aguguom et al. (2023) said that efficient mobilization of IGR enhances the budgetary capability for public capital projects. These consistencies validate that improved internal revenue efforts promote infrastructure development, as shown by actual data.

Nonetheless, some studies have presented divergent viewpoints. Wablah et al. (2024) argued that heightened IGR does not necessarily lead to increased capital expenditure due to issues such as misallocation, corruption, or inefficient expenditure management. Evidence indicates that improving the effective collection and management of domestically generated funds will facilitate increased infrastructure development in Nigerian states (Alakija et al., 2025). This aligns with the notion that fiscal capacity, driven by internal revenue systems, is vital for public investment and developmental outcomes.

CONCLUSION

The paper analyzes the effect of internally generated revenue (IGR) on the capital expenditure of the southwestern states of Nigeria. The analysis indicates a significant relationship between internally generated revenue (IGR) and the development of capital expenditure in the southwestern states of Nigeria. Hence, efficient tax collection and enhanced revenue mobilization are crucial for financing infrastructural projects that are fundamental for sustainable development.

Both taxes and earnings have a positive and significant effect on capital expenditure in southwest Nigeria. This suggests that public sector capital expenditure increases alongside enhancements in internal revenue streams. Fees and fines have a negative and significant influence on capital expenditure. This indicates that an increased reliance on these revenues may hinder the government's ability to invest effectively in public infrastructure and services. Locally generated resources are essential for fostering development investment, as evidenced by their statistical significance and considerable explanatory power in the regression analysis.

Based on the findings, the following recommendations were made. The government should focus on key components of IGR, such as tax, fines, fees, and earnings and sales, to address the shortfall in IGR. The government should recognize the significant correlation between IGR and CAPEX, demonstrating their consistent movement in tandem over time. A rise in capital expenditure is associated with higher domestic income. It is vital to prioritize revenue mobilization tactics, as historical IGR values serve as significant indicators of current capital expenditure levels. Boosting internal revenue generation mechanisms through taxation reform, compliance, and administrative efficiency will significantly influence the capacity for infrastructural development.

Future research should employ longitudinal datasets and causal inference techniques, as it is necessary to confirm these relationships. Furthermore, future studies might explore whether these relationships are mediated by overall governance quality or macroeconomic stability, broadening the understanding of how IGR can effectively drive infrastructural development.

AUTHOR CONTRIBUTIONS

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