Policy Brief

Impact of Monetary Policy on Companies Income Tax Revenue in Nigeria:

Threshold Regression Approach

PUBLISHED

BY

RESEARCH AND STATISTICS DEPARTMENT (RSD)

Introduction

Monetary policy plays a critical role in shaping corporate income tax (CIT) revenue in Nigeria. This study, which was carried out in 2024, investigates the long-term relationship between key monetary policy variables (exchange rate, inflation rate, interest rate) and CIT revenue. A threshold regression model (TRM) approach was used to analyze the impact of these variables on CIT over the period 1995 to 2022. The average threshold values for these variables are: N307/USD, 8.5%, 9.8%, and 15.7% for exchange rate, interest rate, inflation rate, and CIT respectively.

Key Findings

The following findings provide insight into how shifts in monetary conditions influence tax performance and broader fiscal outcomes:

- The study confirms a long-term negative and statistically significant relationship between CIT revenue and each of the monetary policy variables. In other words, when the threshold levels of the three monetary policy variables are exceeded, the CIT revenue will be impacted negatively. i.e an increase in each of the monetary policy variables will lead to a decrease in CIT revenue.

- In addition to these monetary policy variables, the study used GDP and Institutional Quality as control variables and found that they positively influence CIT revenue. This is not suprising as a boost in GDP will lead to an increase in profitability of companies which will in turn generate higher CIT revenue. It should be noted, however, that the effect of these variables on CIT revenue is statistically insignificant.

Policy Recommendations

1. **Regular Monitoring:** Federal Inland Revenue Service should track fluctuations or movements in Exchange Rate, Interest Rate, Inflation Rate and other key economic fundamentals to assess their impacts on CIT revenue.
2. **Fiscal-Monetary Coordination:** There is a need to strengthen collaboration between fiscal and monetary authorities to ensure policy coordination and coherence in order to mitigate adverse effects of some monetory policy decisions on tax revenue. In other words, there should be regular handshakes between the CBN, FIRS and other relavant stakeholders.
3. **Institutional Quality Improvement:** Government should continue with its transformation agenda to improve governance and institutional efficiency aimed at enhancing CIT revenue.