Economic transformation for subnational IGR growth

STATES & LOCAL FINANCE

The IGR Initiative

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A SIMPLE FORMULA FOR SOLID IGR performance is to consistently grow the economy at a robust rate and strengthen the institutions for revenue mobilisation for effectiveness and efficiency. It is a no-brainer as every progressive leader ideally should know this. However, if we know the ingredients for sustainably growing the IGR, why does financial distress seriously threaten our governments? The answer lies in the absence of a "plough back mentality." All great entrepreneurs know that they must profitably reinvest the surplus cash and a reasonable proportion of the residual income from that enterprise for it to grow at the desired rates. They must be replacing old machines, deploying modern technologies, building workforce capacity, expanding new sites, and continuously fine-tuning their business processes. Ploughing back earned income enables the continuous actualization of these entrepreneurial desirables. This principle is not exclusive to entrepreneurs. The truth is that the government must operate like an entrepreneur, living out the principles that make entrepreneurship create prosperity.

That way of life wins as it not only means that the government directly enjoys the accruing advantages of efficiency but fosters a better understanding of how the investment sector functions. Economic growth is assured chiefly with a robust investment sector and the resulting array of entrepreneurial activities, output, and employment. Earnings from these activities, the profits and income from the employed workforce yield the IGR. Consequently, the financing of the public goods and other supporting infrastructure, including sound security management that provides the fertile environment for business growth, proceeds from prudent ploughing back of these mobilised revenues. This dynamic circular relationship must receive adequate nourishment so that the economy can flourish and deliver revenue in abundance to the government. Today, both sides appear to be flat on the ground. Therefore, given the severity of the threats of fiscal distress that over 80 percent of Nigeria's subnational governments contend with and the equally challenging economic conditions that individual and corporate economic agents face, the question is, which side is to be activated first in order to restore a sound circular flow.

Some analysts who lean on one of the many extended interpretations of the so-called social contract theory believe that the taxpayers who appear to have conceded much of their rights to the government should persevere in complying with their tax payment obligations despite the challenging times. Those who believe citizens have the right to demand accountability even through extreme protest, including tax evasion, argue differently, albeit within the same theoretical context. Their opposition is that the government should demonstrate substantial goodwill by utilising previously paid taxes and collected revenue to fertilise the business environment and make businesses and the investment sector flourish before demanding new tax payments. Although this is a theoretical argument, as the government keeps providing public goods while economic agents continue to pay taxes and make fresh investments, it is relevant for understanding each player's importance in the sequence of events in delivering economic growth and IGR expansion. The practical truth is that the most productive way to grow a plant is to prepare and manure the soil that hosts it appropriately.

The capacity to substantially reverse the damage to subnational revenue independence and growth caused by crude oil discovery exists. Although the world has gone beyond mere primary production and nature-given dominant economic structures, we can still revamp the groundnut pyramids and the cocoa colonies and explore other viable natural endowments. We can stimulate the demand for our nature-given resources and consciously create and strengthen supply chains that facilitate speedy development across the country. This exploitation of economic potential is a natural burden that most political leaders at the state and local government levels, either naively gloss over or fail to mobilise the needed capacity to explore because of the monthly statutory federation account allocation.

Fortunately, several options are open to chief executives of states and local governments to expand profitable economic activities sustainably. Regardless of the adopted routes, few but critical considerations consistently delivering good outcomes must receive priority attention. We know from basic economics that there is hardly any state and local government that does not possess a tremendous comparative advantage in producing one or several commodities. The same economics teaches us that the adequacy of land and raw materials, human capital, technological and financial capital, an effective justice system and entrepreneurship would primarily facilitate goods production. Additionally, appropriate supply chain infrastructure linking these outputs to demand sources would ensure that these production engines are continuously at work. Chief executives of subnational governments can play unique roles in identifying these comparative advantages and ensuring the adequacy of some of these factor resources that make production possible in their domains are of the right quality and quantity. Some of these factor resources would naturally prop up the supply chain infrastructure linking the supply to demand.

Success in this process of essentially leveraging natural endowments to orchestrate transformations in secondary and tertiary sectors is the surest path to subnational fiscal diversification. To identify areas of comparative advantage, subnational governments may need to score each target sector based on four critical considerations, namely [a] firm profitability and growth prospects within the subsector, [b] financing requirements for operating successfully within the subsector, [c] human resource availability, technology, and supportive environment and [d] government's policy disposition to attracting the right set of investors. Inarguably, the higher the score in sub-sector profitability, the better a candidate is for entrepreneurial expansion if developed. However, if the financial requirement to set up operations in the sub-sector is too much for an average entrepreneur, the government may step in through different channels. Examples of such channels include design-build-and-divest, credit guarantees for primed potential investors or the establishment of special purpose vehicles for assembling investors to co-own such operations. In addition to these challenges are technology and workforce, which must be in the correct quantity and quality. Subnational governments desirous of achieving this transformation would assign appropriate weights for these four criteria based on their particular contexts and then use them to score each subsector.

Therefore, the first assignment is identifying areas of comparative advantage, channels of financing support, the size and calibre of human capacity requirements, and supply-chain support infrastructure. Most progressive subnational governments would go even further in noting and installing infrastructure that investors would find irresistible. For instance, the setting up of industrial and technology hubs with all perquisites for successful business operations such as electricity, solid and well-maintained road connections linking markets and ports, among other incentives, such as reasonable tax holidays, have become popular. It is an easy decision, that any well-meaning government, desirous of expanding its internally generated revenue on a sustainably growing basis, must plan its fiscal spending programmes around these identified needs. This process has multi-barrel positive effects on labour quality and mobility, technological progress, scaling up of agricultural and mineral mining activities and, ultimately, massive growth of the secondary and tertiary sectors. The more manufacturers are assured of the adequacy of raw material supply with a suitable business environment, the more they plant their operations. Expansions in the size of embedded services ride on the back of buoyant growth in the primary and secondary sectors.

How quickly these initiatives deliver the desired outcomes depends on the effectiveness of programme sequencing. Ideally, in identifying areas of comparative advantage, low-hanging fruits that can start yielding satisfactory results receive priority attention. Political leaders desirous of celebrating their first 100 or 200 days would find that prioritised sequencing with low-hanging fruits takes precedence. Of course, the entire economic transformation programme must follow realistic timelines. There is no need to force projects that can be completed in the medium term into the short term unless unforeseen constraints such as a lack of funds exist. In the same vein, it is wasteful to stretch projects and programmes deliverable within the short-term into the medium or long-term.

The second and crucial leg of this model of economic transformation for an enhanced IGR is the efficiency and effectiveness of the revenue-mobilising ecosystem. Although the core of this system lies within the tax administration, it is extremely limiting to focus on the IRS in the pursuit of robust IGR expansion. Internally generated revenue efforts should transcend the IRS's institutional capacities, albeit retaining the coordination rights. For example, as per the law, taxpayers must comply or face the penalties as stipulated. Unfortunately, the arms of the law at most subnational levels suffer significant paralysis and cannot catch most of the supposedly big tax revenue contributors-but-evaders. Most of these VIP taxpayers are usually cronies of the governors and chief executives of local governments. Therefore, tax administration efforts would not yield much fruit unless the governor puts his foot down. We also know about the many ramblings between tax administrations and other revenue-collecting ministries, departments and agencies of government who consistently fail to deliver revenue collected correctly. Despite these challenges, there can never be any substitute for strengthening tax administrations at the subnational level. Implementing a globally accepted tax administration diagnostic assessment tool and using inferences from the scores to design robust IGR expansion programmes is instructive.

Finally, the winning rule in this economic change game is focusing at every given time on critical priorities and ensuring that the key success drivers to accomplishing them are adequately in operation. Governance attracts hordes of distractions falsely capsuled as essential suggestions. Without the leader's attention on those economic growth considerations that matter most, the undeniable endpoint would be the miry clay of unimpactful programmes and projects. The capacity to achieve this level of attention on what matters most often depends on the depth of knowledge in entrepreneurial leadership and economic management. Those elected to positions of political authority must take time to steep themselves deeply in those areas of knowledge. They should also surround themselves with those who understand how it works and possess the discipline required to call them into action.

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