Impact of Revenue Allocation on Economic Growth in Nigeria (1981-2016)

Onyia, Chinedu Callistus[1] and Okereke, Samuel Felix[2]

[1]Department of Banking and Finance Enugu State University of Science and Technology, Enugu, Nigeria.
[2]Federal University Dutsinma, Katsina State, Nigeria.

Email: justonyia@yahoo.com, sokereke@fudutsinma.edu.ng

ABSTRACT

This study was state to investigate the impact of revenue allocation on economic growth in Nigeria using time series data from 1981 to 2016. The ex post facto research design was employed in the study which necessitated the use of the augmented unit root test, Cointegration test and the Error Correction Model to analyze the data. Revenue allocations to two levels of government were used as independent variables while real gross domestic product represents economic growth. The study major objectives of the study are to determine the impact of federal government revenue allocation share on economic growth in Nigeria. And to determine the impact of state government revenue allocation shares on economic growth in Nigeria. The study found that revenue allocations to the federal government has a significant positive impact on economic growth in Nigeria for the period studied. Also, revenue allocations to the state governments has a significant positive impact on economic growth in Nigeria for the period studied. Therefore, the study recommends that the continuous agitation for more revenue allocation to states should be reviewed properly by federal government and state governments to ensure a sustained increase in of direction of the impact of it on real GDP.
Keywords: Impact, revenue, economic growth and allocation.

INTRODUCTION

Background of the Study

Government revenue refers to the revenue received by a government to finance its day to day activities and carry out developmental projects. It is an important tool of the fiscal policy of the government as it facilitates government spending [1]. Governments need to perform various functions in the field of political, social and economic activities to maximize social and economic welfare. In order to perform these duties and functions government require large amount of resources which are referred to as public revenues. However, Nigeria is a mono-economy with her revenue base mainly from the oil sector, especially, in terms of the federally collected revenue. For instance, oil revenue constitutes greater part of federally collected revenue and each of the different levels of government depends largely on its share of the federally collected revenue to carry out its functions.

Thus, most of the states depend mainly on their shares of federal allocations to carry out their functions. The revenue allocation formulae now in use came into effect on 10 July 1992 with the promulgation of the "allocation of revenue (Federation Account etc) (amendment) decree of 1992. It provides as follows: 48.5% for Federal Government, 24% for the state governments, 20% for local government, and 7.5% for Special fund [2].

Thus, Nigeria as a nation operates a federal structure of government. Federalism refers the existence in one country of more than one level of government, each with different expenditure responsibilities and revenue powers [3]. This shows that fiscal federalism, a consequence of federalism, is all about the relationship among the different units of functions and revenue powers to the constituent units. The existence of imbalance between functions and resource base makes it important for the higher level of government to transfer revenue to the lower level which is referred to as efficiency transfer or balancing [4].

Meanwhile, the sharing of funds from the federation account is one of the contentious and sensitive issues in the Nigeria polity this has remained a central element of inter-fiscal relations. In Nigeria revenue allocation is taken as the distribution of national revenue among the various tiers of government in the federation in such away as to reflect the structure of fiscal federalism. This issue is so important that in some other countries it has become a national question [5]. It is so important because it has serious implication on the level of economic growth of the country. In Nigeria in recent years for example, many states have run to the center for their share of the revenue not minding the growth pattern of the economy. It then become necessary to study the impact of the revenue allocation method on the Nigerian economy.

STATEMENT OF PROBLEM

Recently, there have been agitations to amend the allocation formulae to favor the states given the argument that states are the level of government closer to the people than the federal government, and therefore, will be more responsive to the particular preferences of their constituencies as they easily find new and better ways to provide these services [6] as cited in [7].

However, the major argument is centered on whether giving states more revenue strength will improve the economic development of the country. Studies on this have been more of narrative and descriptive, few have been empirical, thus, it becomes necessary to examine if the allocations to the states have contributed to economic growth in Nigeria.

Research Objectives
To determine the impact of federal government revenue allocation share on economic growth in Nigeria.
To determine the impact of state government revenue allocation shares on economic growth in Nigeria.

Research Questions
To what extent does federal government revenue allocation share impact on economic growth in Nigeria?
To what extent does state government revenue allocation share impact on economic growth in Nigeria?

Research Hypothesis
Federal government revenue allocation share has no significant impact on economic growth in Nigeria.
State government revenue allocation share has no significant impact on economic growth in Nigeria.

SCOPE OF THE STUDY

The study covers the period 1981-2016, the base year is chosen to reflect the period of revenue boom from the oil sector in Nigeria.

Significance of the Study
Government and Policy Makers
The study will guide the government to take proper decision on the recent call for revenue allocation review.
Researchers and Students

The study will help researchers and students to update their knowledge gap as it concerns the issue of revenue allocation and economic growth.

LITERATURE REVIEW

Theoretical Literature
Revenue allocation is expected to grow the economy as explained by growth theories.

Solow Growth Theory
The neoclassical economists are instrumental in the development of the growth theory. [8] develops a growth model called the Solow model that explains that the long-run rate of growth is exogenously influenced by the rate of technical progress. Whereas [9] establishes the Harrod-Domar model in which the long-run growth rate is exogenously determined by the savings rate in an economy.

Endogenous Growth Theory
Modification of the neoclassical growth theory became possible due to its shortcomings: the inability of the growth model to explain savings rate and rate of technological progress as exogenous factors. A new growth theory was introduced in the early 1980s as endogenous growth theory [10].

Endogenous growth theory says that economic growth depends primarily on endogenous factors, such as human capital, innovations, knowledge, and positive externalities [11]. The endogenous growth theory holds that policy measures within an economy, such as revenue allocations positively influence the long-run growth rate of an economy, such as increase in real GDP. This study adopts the endogenous growth theory/model for its analysis.

EMPIRICAL LITERATURE

[12] did a study on revenue allocation formula and its impact on economic growth process in Nigeria. The analysis revealed the extent to which revenue allocation formula adopted in the past had affected the path of economic growth and development in Nigeria. The data was purely secondary data and was sourced from the World Bank publication, CBN, Journal and other published and unpublished materials. There was need, therefore to address the problem by formulating a more efficient revenue allocation wastage and mismanagement of funds. Also effort should be geared towards articulation of policies that will enhance capital formulation, employment of the abundant and measures may include attachment of more weight to the share of local government from the federal collected revenue, placing more emphasis on the internal revenue generation, redefinition of the concept of definition and sustaining the present effort of government as regards budget monitoring and implementation.

[13] studied tax revenue and economic development in Nigeria using a macro econometric approach. They examined the impact of tax revenue on the economic growth of Nigeria, judging from its impact on infrastructural development from 1980 to 2007. To achieve this objective, relevant secondary data were collected from the Central Bank of Nigeria (CBN) Statistical Bulletin, Federal Inland Revenue Service (FIRS) and previous works done by scholars. The data collected was analyzed using the three stage least square estimation technique. The results showed that tax revenue stimulates economic growth through infrastructural development. That is, it highlights the channels through which tax revenue impacts on economic growth in Nigeria. The study also reveals that tax revenue has no independent effect on growth through infrastructural development and foreign direct investment, but just allowing the infrastructural development and foreign direct investment to positively respond to increase in output. However, tax revenues can only materialize its full potential on the economy if government can come up with fiscal laws and legislations and

strengthen the existing ones in line with macroeconomic objectives, which will check-mate tax offenders in order to minimize corruption, evasion and tax avoidance. These will bring about improvement on the tax administration and accountability and transparency of government officials in the management of tax revenue. Above all, these will increase the tax revenue base with resultant increase in growth.

[14] empirically examines the impact of revenue allocation on economic development in Nigeria. Specifically, the study looks at how the various revenue allocations to the three tiers of government affect real gross domestic product (RGDP) in Nigeria using time series data for the period 1993 to 2012. Error correction model (ECM) and Pair wise Granger Causality test are used in analyzing the data. The study carries out test of stationarity of the variables using Augmented Dickey–Fuller unit root test and test of long-run relationship among the variables using Johansen Cointegration test. The study's findings show that revenue allocations have significant causal relationship with economic development in Nigeria, with only revenue allocation to states having significant negative relationship. Unidirectional causality runs from revenue allocations to real
GDP in Nigeria. All variables of the study are cointegrated and have a long-run relationship that 87.62% of the short-run disequilibrium is corrected yearly. The study recommends among others that more financial control and value for money audit should be carried out to minimize wastages and corruption in the states of the federation, so as to change the direction of influence of states' revenue allocation on economic development.

[11] analyzed the extent to which revenue generation had affected the development of the selected local Governments. The researcher used both primary and secondary methods of data collection to generate the needed data. The data

obtained through secondary data were analyzed using simple least square regression method. The following were some of the findings which included the following; there is a significant relationship between revenue generated and developmental effort of government, poor development of the areas, lack of basic social amenities to the rural people and lack of revenue to maintain the existing infrastructures. The researcher therefore recommended that the local government should provide basic amenities of high quality. By doing so, the people's interest would be geared towards giving their maximum support to the local government which would lead to the development of the rural area

[7] examines the relationship between government revenue and economic growth in Kenya. The study adopted a descriptive research design. The study used secondary data collected from the Central Bank of Kenya, KNBS, KIPPRA, and Ministry of Finance, Public libraries and National Budget and other Government records including import duty, excise duty, income tax and Value Added Tax (VAT) which comprised the tax revenue. In addition, the study collected data on non tax revenue. The study concludes as import duty increases the economic growth declines and vice versa. With regard to excise duty, this study concludes that as increase in excise duty slows reduces the rate of economic growth. On Income tax, the study concludes that established Income Tax leads to continuous increase in revenue obtained by government. The study further concludes that there is a direct relationship between Income tax and economic growth. The study concludes that increase in VAT leads to positive effects on the rate of economic growth. The study concludes that there is a relationship between government revenue and economic growth but at a slow pace.

[3] this study investigated the time series role of non-oil revenue variables on economic growth in Nigeria. This study thus extends the literature in this area by

employing cointegration methodology alongside error correction mechanism to investigate the impact of non-oil revenue on economic growth in Nigeria. The study employed annual observations from 1980 to 2013. The non-oil revenue variables analyzed are: agricultural revenue and manufacturing revenue. Results show that agricultural revenue, manufacturing revenue and interest rate have significant impact on economic growth in Nigeria. Results also show the existence of long-run equilibrium relationship and short run dynamic adjustment with speed of about 52% to restore equilibrium.

[13] investigated the growth impact of the federation allocation shares (federal and state governments) and state governments' internally generated revenue in Nigeria, for the period 1970-2009, using the distributed lag model. After studying the time-series properties of these variables for stationarity, a dynamic model was estimated. The regression result suggests that, in the long run, growth can be influenced positively by the share of the federal government allocation and the state governments' internally generated revenue. In the contrary, result suggests that state governments' allocation share has negative impact on economic.

Gaps from previous reviewed literatures

Research Design
The study will use the *Ex Post Facto* Research Design. This is necessary because the study will use existing data to predict future outcomes. The study will make use of the econometrics research design for addressing the objectives of the study. The researcher will adopt the multiple regression analysis based on the classical linear regression model, otherwise known as Ordinary Least Square (OLS) technique to analyze the objectives. For the econometrics model, the specification of the model is based on the empirical work of [9].

Nature of the Data

A summary of the above reviews have emphasized more on public expenditure pattern or on the effect of oil revenue on the economy. But one notable issue from the review is that government budgetary spending measures tested in the literatures are the total government expenditures or total expenditures expressed as percentages of GDP. This study has decomposed government expenditure into sectors to know which of them react more to oil revenue fall. This approach constitutes one of the new additions to the literature compare to past studies.

Several related studies reviewed neglected the fact that the effect of revenue decline in Nigeria do not react equally and at the same time to all the sectors. Therefore aggregating the expenditure data leads to wrong conclusion. Also, this study contributes to knowledge by using the key sectors needed to revamp the Nigerian economy (Agricultural, education and health) and which have been falling behind other sectors in terms of their public expenditure allocations to know their reactions to revenue fall in the country.

Moreover, the study extended the time series data range used in the study to 2015 to account for recent changes in the economy which other studies did not take account of.

METHODOLOGY

The data is a time series secondary data showing aggregate data for the Nigerian economy. Apart from population growth rate in percentages, all other variables will be in N millions.

Model Theoretical Backup
However, this study adopts the endogenous growth theory for its analysis. The model advocated for a positive relationship between revenue and economic growth.

Model Specification
In this study, four hypotheses have been stated with the view of assessing the impact of global economic shocks on exchange rate fluctuation in Nigeria's

economy (1981-2016). The models of this study are based on the model of [11]. An econometric Analysis, of which gross domestic product is the dependent variable while the independent variables are variables like federal government revenue share, state government revenue share and state internal revenue. The model is stated below;

$$Y = F (X_1, X_2, X_3, \ldots \ldots X_n) \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ 1$$

where
Y = is the regressand
$X_1 \ldots X_n$ are regressors
F is the functional notation, equation (**1) will be stated econometrically as;**
$$Y = ß_o + ß_1 X_1 + ß_2 X_2 + ß_3 X_3 \ldots\ldots ßnXn \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ 2$$
Where
Y = as stated above
$X_1 \ldots\ldots X_n$ as stated above

$ß_{1\ldots\ldots}ßn$ **(scope) parameters of the regressors**
$ß_o$ **= intercept.**
μ_i = error term
Equation (**2) is transformed to reflect the variables used in this study a**s stated below;
RGDP = $ß_o + ß_1$ FGREV+ $ß_2$SGREV + $ß_3$SIGR+ μ_i \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots**4**
RGDP = Real Gross Domestic product proxy for economic growth).
FGREV= Federal Government Revenue Share
SGREV = State Government Revenue Share.
SIGR = State Internal Generated Revenue
Where,
$ß_1 > 0; ß_2 > 0; ß_3 > 0$

Error correction model
After the regression, the error will be added to the model to check the speed of adjustment between the long-run and the short-run model. This will be done following the Granger Representation Theorem which stated that if two variables Y and X are cointegrated, the relationship between the two can be expressed as ECM [9].That is

$$\Delta RGDP_t = \beta_{0+}\beta_1 \sum_{i=1}^{n} \Delta FGREV + \beta_2 \sum_{i=1}^{n} \Delta SGREV + \beta_3 \sum_{i=1}^{n} \Delta SIGR + \beta_4 ECM_{t-1} \ldots\ldots\ldots\ldots\ 7$$

The coefficient of the error correction (ECM_{t-1}) will indicate the percentage of the error corrected each year that is, the speed of adjustment.

Technique of data analysis
The modelling procedures adopted in this study are as follows:
  I.   The investigation shall be carried out in a linear form, using the OLS method estimating a multiple linear regression of the variables in equation
  II. Determining the suitability of the variables for a time series regression using Augmented Dickey Fuller (ADF) unit root test for stationarity.

  III. If the variables tested in (ii) above are all suitable at the same level, then they are subjected to a uniform adjustment to equilibrium known as cointegration test.
  IV. Should co-integration exist the ECM model is estimated where the speed of adjustment to equilibrium will be determined and diagnostic tests conducted.

Justification of the Model

This research work will employed Ordinary Least Square (OLS) estimation because of its

reliable qualities as the best unbiased estimator and because the equations were in recursive form. Since the focus of the study is to establish the link between financial intermediation and growth, based on the aforementioned theoretical postulates and following the practices in most studies, an appropriate technique is to adopt the error correction modelling (ECM) and co-integration approach popularized by Engel-granger. This will enable us to establish the stability of the model and the movement pattern of the variables towards equilibrium and to speed of adjustment from short-run to long-run.

Data Sources
Annual secondary data sourced from the 2016 Central Bank of Nigeria statistical bulletin covering the period 1981-2016 will be used in this study.

Econometric Software
E-views version 9.0 will be used for model estimation in this study.

ANALYSIS AND PRESENTATION OF RESULTS

Analysis of Results
Data Presentation
The data used for the regression is presented below.
Source: 2016 Central of bank of Nigeria, statistical bulletin
Unit root tests and the order of integration.
Tables 1 below presents the summaries of the unit root test results for the series in levels and first differences. The result indicates that all the variables were non-stationary at levels since there ADF statistic absolute value did not exceed the critical values, thus were differenced. Furthermore, the results in Table 1 indicate that four of the variables in each of the unit root test below become stationary at first difference.

Table 1   ADF Unit root test results of the series in levels and difference

Variable	Test at levels			Test at 1st difference		
	ADF stat.	Constant & Trend	5% critical level	ADF stat.	5% critical level	Remark
FGREV	0.615293	Constant	-1.952066	-4.812567	-3.622033	Stationary at I(1)
SGREV	-0.677992	None	-1.952066	-5.790438	-1.952473	Stationary at I(1)
SIGR	1.834487	None	-1.952066	-4.984488	-2.963972	Stationary at I(1)
RGDP	3.172638	None	-1.951000	-5.980119	-2.954021	Stationary at I(1)

Source: Computed by the Author
Having established that all the series are stationarity at the same order I(1), therefore we proceed for cointegration test.

Cointegration Test
Table 2 Residual based cointegration Test

Variable	ADF-test statistics	5 % critical value	Outcome
Residual	-4.098450	-2.952066	Cointegration

Source: Computed by the Author

Interpretation

Table 2 is the co-integration test result which came about because the variables used in this study were not stationary at levels, using them in that form will mean a spurious regression, since they became stationary at first difference, their combined form need to be stationary too for easy adjustment to equilibrium. Cointegraion test become necessary in order to check if the linear combination of the variables will be stationary. The result show that the three models passed the cointegration test since the saved residual unit root is stationary using the Engel-granger two-step cointergraion method; this implies that there will be Error Correction Mechanism. Therefore this study will proceed to long and short run analysis between oil price fall and the composition of budgetary allocations in Nigeria across the selected sectors.

Short run Evaluation of the estimated Regression Model One
Table 5: The ECM

Dependent Variable: RGDP

Independent Var	Coefficient	Std. Error	T-statistics	Probability
C	-1043.848	3093.924	-0.337386	0.7386
FGREV	0.004844	0.001745	2.775496	0.0103
SGREV	620.6426	148.9038	4.168079	0.0003
SIGR	-0.080011	0.084577	-0.946012	0.3532
ECM	-0.971728	0.159282	-6.100677	0.0000

Source: Computed by the Author

R² = 0.731542; Durbin – Watson =1.922913; F-probability = 0.000002

The short run result shows that a unit increase in federal collected revenue will lead to 0.004 increases in economic growth, meaning that there is a positive relationship between federal collected revenue and GDP. State collected revenue share result shows that if state revenue increases by a unit, real gross domestic product increases by 620 units. State internal generated revenue result show negative relationship with real gross domestic product though it's not statistically significant and this does not conforms to a priori expectation. Economically and statistically federal collected revenue and state collected revenue are significant by conforming to a priori expectation and greater than 5% probability test of significance respective, while state internally generated revenue is not significant economically and statistically given the results above.

The Error Correction Term is significant and appeared with the negative expected sign, which means that 97% of the deviations in equilibrium in the short-run are corrected in the long run annually.

Again the **R²** result of **0.73 (73%)** shows that there is a strong goodness of fit between real GDP independent variables, while D.W Stat of 1.9 and **Prob(F-Stat) = 0.000002** show no autocorrelation among

the variables and overall statistical significance respectively.

Economic criterion (Short run Result)
This criteria is used to examine whether the regression parameter coefficients agrees with theoretical postulations or conforms to a priori expectations in sign. Table 6 shows whether the economic variables under study conform to a priori expectations or not in the short-run.

Table 6: Economic Criteria

Variables	Actual Sign	Expected Sign	Remark
FGREV	Positive	Positive	Conformed to a priori
SGREV	Positive	Positive	Conform to a priori
SIGR	Negative	Positive	Did not Conformed to a priori

Source: Authors Computation

The result in the table above implies that all the variables obeyed their economic criteria, apart from the SIGR in the short run.

Analyzing the Test of significance
This test is carried out in order to check how the independent variables significantly affect the dependent variable. In other words it tests the statistical significant of the estimated parameters at 5 percent level of significance (α =5% (0.05). the overall Prob(f-statistic) value will be used to justify the study hypothesis at 5 percent level of significance (α =5% (0.05).

Decision criteria
If the probability of the independent variable is less than the chosen probability level of significance, then reject the null hypothesis and accept the alternative hypothesis and conclude that the variable in question is statistically significant at 5% level and is a good explanatory variable of the dependent variable. If otherwise, then the variable is not statistically significant at 5% level and is not a good explanatory variable of the dependent variable. The table below presents the regression result and their assessment of significance based on prob(F-stat).

Test of Hypothesis
Hypothesis 1
Federal government revenue allocation share has no significant impact on economic growth in Nigeria.

Hypothesis 2
State government revenue allocation share has no significant impact on economic growth in Nigeria.

Result used in testing hypotheses

Dependent Variable: AGRICEXP

Independent Var	Coefficient	Std. Error	T-statistics	Probability
C	-1043.848	3093.924	-0.337386	0.7386
FGREV	0.004844	0.001745	2.775496	0.0103
SGREV	620.6426	148.9038	4.168079	0.0003
SIGR	-0.080011	0.084577	-0.946012	0.3532
ECM	-0.971728	0.159282	-6.100677	0.0000

R² = 0.731542; Durbin – Watson =1.922913**; F-probability =** 0.000002

From the above table, since the probability value of the independent variable (FGREV) is 0.0103 which is less than the 0.05 probability level for a significance level, therefore the null hypothesis is rejected and the alternative hypothesis accepted which implies that federal government revenue allocation share has a significant impact on economic growth in Nigeria.

Also, the probability value of the independent variable (SGREV) is 0.0003 which is less than the 0.05 probability level for a significance level, therefore the null hypothesis is rejected and the alternative hypothesis accepted which implies that state government revenue allocation share has a significant impact on economic growth in Nigeria.

The regression equation ($Y = Bo + B_1X_1 + B_2X_2 + B_3X_3 + B_4ECM_{t-1} + \varepsilon$) is: $Y = -1043.848 + 0.004844FGREV + 620.6426SGREV - 0.080011SIGR -0.971728ECM_{t-1}$

As per the regression equation established, there was a direct relationship between Economic Growth and federal government revenue share and state government revenue share. However there was an inverse regression relationship between Economic Growth and state government internal generated revenue. Two of the predictor values were significant as the probability values

corresponding to these predictor variables were less than $\alpha=5\%$. The constant was -1043.848 indicating that in normal circumstances, Economic Growth in Nigeria will decrease by 1043.848 if there is no revenue shared among the arms of government.

Statistical criteria (first order) TEST
The statistical criteria take into account of the following, prob(F-stat), probability test and R^2 values. The prob(F-stat), and probability test has taking care of the explanatory power of the independent variables as mentioned above, R^2 are examined here;

(a) The coefficient of multiple determinations (R^2).
The R-square (r^2) measures the goodness of fit of a model. It gives the proportion or amount of total variation in the regress and (dependent variable) that is explained by the regressor (independent variable). From the empirical analysis, it was observed that the coefficient of determination (R^2) value is 0.73 and this implies that in the short run approximately 73% of the changes in economic growth in Nigeria are caused by the independent variables (revenue allocation share to the different levels of government).

SUMMARY OF FINDINGS

This study was state to investigate the impact of revenue allocation on economic growth in Nigeria using time series data from 1981 to 2016. The *ex post facto* research design was employed in the study which necessitated the use of the augmented unit root test, cointegration test and the Error Correction Model to analyze the data. Revenue allocations to two levels of government were used as independent variables while real gross domestic product represents economic growth. The study major objectives of the study are to determine the impact of federal government revenue allocation share on economic growth in Nigeria. And to determine the impact of state

government revenue allocation shares on economic growth in Nigeria.
The study made the following findings:
i.   Revenue allocations to the federal government has a significant positive impact on economic growth in Nigeria for the period studied.
ii. Revenue allocations to the state governments has a significant positive impact on economic growth in Nigeria for the period studied.
The policy implication of the study is that during the period under review, the share of federal and state government from the federation account contributed to the economic growth process of Nigeria.

Hence the share of state government must be increased for improved performance. This is consistent with the findings of [7]. However, the state internal generated revenue did not perform as expected.

Hence, effort should be geared towards effective and efficient utilization of fund at the state level. The scenario at the state level may be due to mismanagement and embezzlement of fund.

CONCLUSION

In this study, we have been able to established that revenue allocation share from federal and state governments has affected the path of economic growth and development in Nigeria. More so, the study revealed that the coefficient of the state revenue share is higher than that of federal. The therefore concludes increasing revenue allocation to the state governments will lead to provision of more goods and services, higher investment and economic growth.

RECOMMENDATION

1. The study recommends that the federal government should make efforts to embark on more developmental projects with their revenue share so as to enhance the growth of the economy

2. The continuous agitation for more revenue allocation to states should be reviewed properly by federal government and state governments to ensure a sustained increase in of direction of the impact of it on real GDP.

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