The Informal Economy, Tax Evasion, and Nigeria's Fiscal Crisis (2015–2025)

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Abstract

Nigeria's fiscal crisis from 2015 to 2025 unfolded against a backdrop of weak domestic revenue mobilisation, macroeconomic volatility, and the dominance of a large informal economy. Despite its position as Africa's largest economy for much of the period, Nigeria recorded persistently low tax to gross domestic product ratios, averaging between 6 and 8 percent, far below continental and global benchmarks. This study examines the relationship between the informal economy, tax evasion, and Nigeria's fiscal crisis during this period, with particular attention to how informality and non-compliance constrained revenue generation and undermined fiscal sustainability. Anchored in Rational Choice and Public Choice Theory, the study interprets tax evasion and informality as rational responses by individuals and firms to weak institutions, low trust in government, and perceived inefficiencies in public spending. Methodologically, the research adopts a qualitative explanatory design based on secondary data, using content analysis of reports from international financial institutions, government agencies, and scholarly literature. The findings reveal that the scale and persistence of the informal economy significantly weakened tax revenue performance, while widespread tax evasion widened the gap between potential and actual revenue, reinforcing chronic fiscal deficits. These revenue gaps translated into adverse fiscal outcomes, including rising public debt, constrained fiscal space, and reduced capacity for developmental expenditure. The study concludes that Nigeria's fiscal crisis cannot be understood solely through macroeconomic indicators but must be situated within the behavioural and institutional dynamics shaping compliance. It recommends strengthening institutional credibility, adopting incentive compatible enforcement, integrating informal activities through graduated formalisation strategies, and aligning revenue reforms with expenditure rationalisation and debt management frameworks to restore fiscal stability.

Keywords: Informal economy, Tax evasion, Fiscal crisis, Public finance, Nigeria, Economic governance

Introduction

Nigeria's fiscal crisis between 2015 and 2025 unfolded within the broader context of structural weaknesses in revenue mobilization, macroeconomic volatility, and a persistently large informal economy. Despite being Africa's largest economy by gross domestic product for much of the period, Nigeria consistently recorded one of the lowest tax-to-GDP ratios globally, averaging between 6 and 8 percent, far below the African average of approximately 16 percent and the OECD benchmark of over 30 percent (International Monetary Fund, 2022; World Bank, 2023). This revenue underperformance has constrained the state's capacity to finance public goods, deepen infrastructure investment, and respond effectively to economic shocks. Central to this challenge is the dominance of the informal economy, which employs over 80 percent of Nigeria's labour force and accounts for more than half of total economic activity, yet remains largely outside the formal tax net (National Bureau of Statistics, 2018; International Labour Organization, 2020).

The research is necessitated by the problem of the Nigerian state's persistent inability to mobilize adequate domestic revenue between 2015 and 2025, largely due to the expansion of the informal economy and widespread tax evasion. The persistence of informality in Nigeria is not merely a transitional phenomenon but a structural feature shaped by historical, institutional, and political factors. Scholars have long argued that the Nigerian state's weak fiscal social contract, characterized by limited trust between citizens and government, undermines tax compliance and reinforces informality as a rational survival strategy for households and firms (Ake, 1981; Fjeldstad and Moore, 2008). Between 2015 and 2025, these dynamics were intensified by economic recessions in 2016 and 2020, foreign exchange instability, and inflationary pressures that eroded real incomes and further discouraged voluntary tax compliance among small and medium enterprises (Central Bank of Nigeria, 2021; IMF, 2023). As economic hardship deepened, tax evasion became increasingly normalized, blurring the line between informal economic participation and deliberate avoidance of fiscal obligations.

The primary objective of this study is to examine the relationship between the informal economy, tax evasion, and Nigeria's fiscal crisis from 2015 to 2025. It seeks to assess the extent to which informal economic activities and tax avoidance practices have constrained domestic revenue generation. The study also aims to analyze the impact of these factors on public expenditure, debt accumulation, and fiscal sustainability. Additionally, it intends to identify institutional and policy challenges that have hindered effective tax administration. Finally, the research aims to provide evidence-based recommendations for improving revenue mobilization and promoting fiscal stability in Nigeria.

Tax evasion in Nigeria operates across both informal and formal sectors, but its effects are most visible in the informal economy, where weak documentation, cash based transactions, and regulatory fragmentation make enforcement costly and politically sensitive. Empirical studies indicate that Nigeria loses billions of dollars annually through uncollected taxes, illicit financial flows, and underreporting of income, with the informal sector accounting for a significant share of these losses (African Development Bank, 2024; Onyekachi and Udeh, 2021). The consequence has been a chronic revenue gap that forced the government to rely heavily on borrowing, with debt servicing consuming over 60 percent of federally retained revenue by 2023, thereby crowding out social spending and capital investment (Debt

Management Office, 2023; World Bank, 2024). This pattern underscores how tax evasion and informality are not peripheral issues but central drivers of Nigeria's fiscal fragility.

Successive governments during the period under review introduced reforms aimed at expanding the tax base and reducing dependence on oil revenue, particularly following the oil price collapse of 2015 and the COVID-19 induced downturn of 2020. Measures such as the Voluntary Assets and Income Declaration Scheme, the expansion of value added tax, and the digitalization of tax administration were intended to improve compliance and integrate informal actors into the fiscal system (Federal Inland Revenue Service, 2021; OECD, 2022). However, evidence suggests that these reforms achieved limited success in addressing the structural roots of informality, as enforcement focused disproportionately on already compliant taxpayers while informal operators remained largely outside effective regulatory reach (Aina, 2023; IMF, 2024). This uneven burden reinforced perceptions of fiscal injustice and further weakened tax morale.

The interaction between the informal economy and Nigeria's fiscal crisis must also be understood within the broader political economy of governance and state capacity. Weak institutions, fragmented regulatory authority, and corruption have undermined the credibility of tax systems, making evasion a rational response to perceived misuse of public funds (Transparency International, 2023; Timmons, 2010). Nigerian scholars argue that citizens' willingness to pay taxes is closely tied to visible service delivery and accountability, both of which remained inconsistent during the 2015 to 2025 period despite rising tax demands (Olaoye and Adereti, 2020; Onyekachi and Udeh, 2021). In this context, informality functions not only as an economic arrangement but also as a form of passive resistance to a state perceived as extractive rather than developmental.

By 2025, the fiscal consequences of prolonged informality and tax evasion had become increasingly evident in Nigeria's constrained policy space. Rising debt, limited revenue diversification, and growing social demands exposed the limits of a fiscal system unable to effectively capture domestic economic activity. The informal economy, while providing livelihoods and buffering unemployment, simultaneously weakened the state's fiscal foundation and its capacity to pursue inclusive development. Understanding the nexus between informality, tax evasion, and fiscal crisis is therefore critical not only for diagnosing Nigeria's revenue challenges but also for informing sustainable fiscal reforms capable of strengthening state capacity and rebuilding the social contract between government and citizens (World Bank, 2024; African Development Bank, 2024).

Conceptual Clarification

The Informal Economy

The informal economy represents a substantial segment of economic activity in many developing countries, and Nigeria is no exception. It encompasses all production, trade, and service activities that are unregulated, unregistered, and untaxed by the state, operating largely outside formal economic institutions. The informal economy is particularly prominent in labour-intensive sectors, such as petty trade, small-scale manufacturing, artisanal services, and agricultural production, which dominate Nigeria's employment landscape. According to the National Bureau of Statistics (2018), over 80 percent of the Nigerian workforce operated within informal economic activities by 2018, contributing more than half of the nation's gross domestic product. Scholars have argued that the informal economy in Nigeria is not merely a transitional or residual phenomenon but a structural feature that reflects deep-seated institutional weaknesses, regulatory fragmentation, and socio-economic constraints (Aina, 2023; International Labour Organization, 2020).

Economic informality has historically served as a buffer against unemployment and economic shocks, providing livelihoods to millions of households who are excluded from formal wage employment. The 2016 and 2020 economic recessions, triggered by the collapse of global oil prices and the COVID-19 pandemic, respectively, intensified informal economic participation, as formal sector employment opportunities declined and households sought alternative means of survival (Central Bank of Nigeria, 2021; World Bank, 2023). Researchers note that this expansion is particularly evident in urban centres such as Lagos, Kano, and Port Harcourt, where informal markets, street vending, and unregistered small businesses dominate commercial activity (Fjeldstad & Moore, 2008; Onyekachi & Udeh, 2021). Despite its role in sustaining livelihoods, the informal economy presents significant policy challenges, particularly in terms of taxation, social protection, and integration into broader economic planning.

From a theoretical perspective, the informal economy reflects the intersection of economic necessity, institutional failure, and social norms. De Soto (1989) posited that informal economic actors often operate outside formal regulatory structures not out of choice but due to excessive bureaucracy, high compliance costs, and limited access to formal credit and land tenure systems. In Nigeria, multiple studies confirm that the informal economy thrives where institutional capacity is weak, regulatory enforcement is inconsistent, and public trust in government institutions is low (Ake, 1981; Timmons, 2010). Informal operators often perceive taxation and regulatory compliance as extractive rather than developmental, particularly in contexts where public service delivery is limited and corruption is prevalent (Transparency International, 2023). Consequently, informality in Nigeria is both an economic strategy and a form of passive resistance to state authority.

The economic significance of the informal sector extends beyond employment. It also represents a critical driver of domestic consumption, urban livelihoods, and entrepreneurial activity. The sector supports backward and forward linkages with formal enterprises, contributing indirectly to industrial and service sector growth, while fostering innovation and flexibility in response to market shocks (International Labour Organization, 2020; African Development Bank, 2024). However, the lack of formal recognition and regulation poses fiscal challenges, particularly for revenue mobilization. Estimates suggest that Nigeria loses billions of dollars annually due to uncollected taxes from informal operators, underreporting of income, and weak enforcement of existing tax laws (OECD, 2022; Onyekachi & Udeh, 2021). The persistence of informality thus has direct implications for public finance, influencing the capacity of the state to fund infrastructure, education, health, and social protection programs.

Studies also highlight the heterogeneity within the informal economy. Not all informal actors evade taxes deliberately; some operate in informality due to barriers to entry into the formal economy, lack of documentation, or limited access to financial services. Small and medium enterprises, artisanal manufacturers, and home-based entrepreneurs often straddle both formal and informal economic spaces, creating complexities for policy enforcement (Fjeldstad & Moore, 2008; Aina, 2023). Moreover, gender dynamics play a role, with women disproportionately represented in informal trade and services, reflecting socio-cultural norms and limited formal employment opportunities (International Labour Organization, 2020). Understanding these nuances is essential for designing inclusive policies that can formalize economic activity without disrupting livelihoods or exacerbating poverty.

Tax Evasion

Tax evasion has been widely recognized as a critical impediment to effective public finance and economic development in both developed and developing countries. It refers to the illegal or deliberate avoidance of tax obligations by individuals, corporations, or institutions, usually through underreporting of income, concealment of assets, misrepresentation of financial information, or non-payment of legally due taxes. In Nigeria, tax evasion has been a persistent challenge, contributing significantly to the low tax-to-GDP ratio, which has historically ranged between 6 and 8 percent, far below the sub-Saharan African average of 16 percent (Fagbade, 2020; Nwosu & Okeke, 2021). Studies indicate that tax evasion is more prevalent in economies with weak regulatory frameworks, high informality, and limited institutional capacity for enforcement, as is the case in Nigeria, where approximately 80 percent of workers operate outside formal tax structures (Ariyo, 2019; Adeyemi, 2021).

Globally, tax evasion is recognized as a major constraint on sustainable development. According to the Organisation for Economic Co-operation and Development (OECD, 2020), developing countries lose an estimated $100 billion annually in tax revenue due to evasion and avoidance, undermining the capacity of governments to provide essential public services. Empirical evidence suggests that the phenomenon is not only confined to high-income individuals or corporations but is widespread among micro, small, and medium enterprises that dominate the informal and formal sectors in Africa. In Nigeria, for instance, research by Adebiyi and Oladipo (2022) highlighted that noncompliance with income tax and value-added tax regulations contributed to an annual revenue loss exceeding ₦500 billion between 2015 and 2020, exacerbating the fiscal stress experienced by the government during economic downturns.

Tax evasion in Nigeria is influenced by structural and behavioural factors. Structural determinants include complex tax laws, multiple tax collection agencies, weak enforcement mechanisms, and a lack of taxpayer education (Olaniyan & Akinlabi, 2020). Behavioural factors encompass low tax morale, distrust in government, corruption, and perceptions of inequitable tax administration (Okafor, 2019; Onuoha, 2022). These factors collectively foster a culture of noncompliance, where taxpayers, especially within the informal economy, perceive evasion as necessary for survival rather than a legal infraction. The COVID-19 pandemic exacerbated these tendencies, as economic contraction reduced disposable incomes and prompted informal and formal sector operators to prioritize business continuity over tax obligations (World Bank, 2022; African Union, 2021).

The implications of widespread tax evasion extend beyond immediate revenue losses. Persistent noncompliance reduces the fiscal space available for critical investments in infrastructure, healthcare, education, and social protection. Between 2015 and 2021, Nigeria experienced chronic budget deficits averaging 3–5 percent of GDP annually, with debt servicing consuming a growing share of federally retained revenue (Debt Management Office, 2022; Ezeani, 2020). This scenario has reinforced dependence on external borrowing and undermined long-term fiscal sustainability, highlighting the structural consequences of unchecked evasion. Researchers argue that such patterns perpetuate dependency cycles, as governments are forced to rely on donor funds, international loans, and commodity exports, rather than building resilient domestic revenue systems (Ariyo, 2019; Fagbade, 2020).

Policy interventions to address tax evasion in Nigeria have been uneven and frequently constrained by institutional weaknesses. Initiatives such as the Voluntary Assets and Income Declaration Scheme (VAIDS) launched in 2017 yielded temporary compliance gains but failed to sustain long-term improvements in revenue collection (Adeyemi, 2021; Adebiyi & Oladipo, 2022). Studies suggest that improving compliance requires a combination of simplified tax procedures, taxpayer education, digitalization of tax administration, effective enforcement, and consistent government accountability (Onuoha, 2022; Olaniyan & Akinlabi, 2020). Comparative analyses indicate that countries that integrated formal sector taxation with incentivized registration of informal operators, such as Rwanda and Kenya, have achieved higher revenue-to-GDP ratios, demonstrating the potential effectiveness of integrated approaches (OECD, 2020; African Union, 2021).

Nigeria's Fiscal Crisis

Nigeria's fiscal crisis between 2015 and 2025 reflects a persistent structural imbalance rooted in the historical formation of the Nigerian state, its resource dependency, and systemic weaknesses in revenue mobilization and public finance management. Ake (1981) observed that the Nigerian state was historically constructed around extractive logics that emphasized rent distribution over productive accumulation, embedding long-standing fiscal fragility. This structural weakness was exacerbated by Nigeria's heavy reliance on oil revenues, which accounted for over 70 percent of federal revenue and more than 80 percent of export earnings for decades, leaving public finances extremely vulnerable to global commodity price fluctuations (Adebajo, 2022). The sharp collapse of oil prices in 2014, compounded by the economic shocks of the COVID-19 pandemic in 2020, led to substantial revenue shortfalls, triggering widening fiscal gaps and exposing weaknesses in domestic revenue mobilization.

The period under review was characterized by recurring budget deficits, as expenditure commitments consistently exceeded government revenue. Federal budgets during these years projected ambitious capital projects alongside escalating recurrent spending on wages, subsidies, and debt service obligations (Ariyo, 2019). IMF reports indicated that Nigeria's non-oil revenue remained persistently low, averaging below 8 percent of GDP despite multiple fiscal reforms, highlighting the inadequacy of domestic revenue collection systems (International Monetary Fund, 2023). To finance recurrent expenditures, the government increasingly relied on both domestic and external borrowing, deepening the debt burden and reinforcing fiscal vulnerability (BusinessDay NG, 2025). This reliance on debt intensified after the 2016 recession and the 2020 pandemic-induced economic contraction, making Nigeria increasingly dependent on borrowing for routine fiscal operations rather than investment in productive sectors.

The escalation of public debt and the growing share of revenue devoted to debt servicing became defining features of the fiscal crisis. While Nigeria's debt-to-GDP ratio appeared moderate relative to global averages, the debt service-to-revenue ratio reached alarming proportions, consuming as much as 97 percent of federal revenue in 2022 and severely limiting expenditure on health, education, and infrastructure (Nairametrics, 2023). World Bank (2024) assessments indicated that much of the borrowing was allocated to recurrent expenditure rather than capital formation, reducing the fiscal space for developmental initiatives. Scholars emphasize that this dynamic entrenched dependency, as limited domestic revenue necessitated external borrowing, further constraining policy autonomy and limiting the state's ability to pursue independent development strategies (African Development Bank, 2024; Adebajo, 2022).

Governance challenges and weak fiscal institutions amplified the crisis. Studies by Ariyo (2019) and others highlight persistent inefficiencies in tax administration, widespread tax evasion, corruption, and fragmented revenue collection mechanisms across federal, state, and local governments. Despite reforms such as the Treasury Single Account and attempts at restructuring tax administration, significant leakages persisted, undermining fiscal consolidation efforts. Subsidy regimes, particularly in the energy sector, consumed substantial portions of public revenue while benefiting limited segments of the population, further reducing fiscal capacity and exacerbating public perceptions of inequitable governance (African Development Bank, 2024). Public distrust in government spending has weakened tax morale, contributing to the persistence of informal economic activity and limiting domestic revenue generation (Taylor, 2019).

Policy measures implemented during this period attempted to address the fiscal imbalance. For instance, the 2025 partial removal of electricity subsidies led to a 35 percent reduction in subsidy spending following tariff adjustments, a measure framed as necessary for fiscal correction but which provoked public resistance (Reuters, 2025a). Similarly, forward-looking fiscal planning saw the approval of a $37.7 billion 2026 budget, with continued reliance on borrowing to cover projected deficits (Reuters, 2025b). IMF projections also highlighted that Nigeria's fiscal deficits averaged above 4 percent of GDP in 2025, signalling structural imbalance rather than temporary shocks (BusinessDay NG, 2025). Such measures demonstrate the tension between fiscal discipline and social acceptability, revealing that sustainable reform requires both institutional capacity and political will.

From a broader political economy perspective, Nigeria's fiscal crisis is intimately linked to the social contract between the state and its citizens. Weak fiscal capacity undermines state legitimacy and reduces compliance with taxation, as governments unable to provide public goods fail to justify tax extraction, further entrenching informal economic activity (Adebajo, 2022; Ake, 1981). Dependency theorists argue that such fragility makes the state susceptible to external pressures, as reliance on foreign financing limits Nigeria's strategic autonomy in international economic and political affairs (Taylor, 2019). Thus, Nigeria's fiscal crisis between 2015 and 2025 cannot be understood in isolation from its structural dependence on oil revenues, weak domestic revenue mobilization, governance inefficiencies, and the broader global economic environment.

Theoretical Framework

Rational Choice / Public Choice Theory

The theoretical lens of Rational Choice / Public Choice Theory offers a powerful framework for understanding how individual behaviour, institutional incentives, and collective decision-making interact to shape economic and fiscal outcomes in states such as Nigeria. Rational Choice Theory itself traces its intellectual roots to the early twentieth century, drawing on classical economic assumptions about human behaviour which posit that individuals make decisions based on a rational evaluation of costs and benefits to maximize their utility (Scott, 2000). Building on this foundational premise, Public Choice Theory emerged more formally in the early 1960s through the work of James Buchanan and Gordon Tullock, who sought to extend rational choice principles into the realm of political science to explain how political actors, bureaucrats, and public officials make decisions (Buchanan & Tullock, 1962). Prior to this formalization, standard economic theory largely treated governments as benevolent entities, but Public Choice scholars instead argue that public sector actors operate with motivations and incentives similar to those in private markets, including self-interest, competition, and strategic behaviour.

Public Choice Theory posits that both citizens and government agents are rational actors who respond to incentives, constraints, and information in ways that seek to maximize their own preferences, whether that be utility, power, or political survival. This perspective fundamentally challenges the assumption of a unified, unitary state working by default for the common good, instead presenting governance as the outcome of competing interests, negotiated compromises, and incentive structures within political institutions (Buchanan, 2000). Central to this theoretical approach is the idea that taxation, public spending, and regulatory policies are themselves the results of bargaining among interest groups, legislators, bureaucracies, and voters, each with differing preferences and levels of influence. In democracies as well as mixed governance systems, this can lead to policy outcomes that reflect not just economic efficiency concerns but the strategic calculations of key actors.

The relevance of Public Choice Theory to the study of Nigeria's fiscal crisis is readily apparent. Between 2015 and 2025, Nigeria struggled with chronic fiscal deficits, weak domestic revenue mobilization, and escalating public debt. Public Choice Theory helps explain why revenue mobilization mechanisms such as tax policy and enforcement have been persistently ineffective: political leaders face competing incentives, including short-term electoral considerations, bureaucratic incentives to protect turf, and public resistance to taxation that is perceived as extractive rather than redistributive (Nweke, 2021). For instance, when the federal government increased value added tax and pursued revenue reforms in the early 2020s, resistance from interest groups and political constituencies diluted the effectiveness of those reforms, resulting in limited enhancement of the tax base and persistent low tax-to-GDP ratios (IMF, 2023). Rather than structural reform, short-term political expediency often guided policy implementation, leaving underlying fiscal vulnerabilities unaddressed.

Public Choice Theory also sheds light on tax evasion and informal economic behaviour in Nigeria. Individuals and firms operating in the informal economy make rational decisions based on perceived costs and benefits of compliance with tax laws. When the costs of compliance, such as complex registration processes, perceived corruption in public spending, and lack of visible public goods, outweigh the benefits of formal participation in the economy, rational actors will choose non-compliance or evasion (Olowofeso, 2022). Rather than viewing tax evasion as purely illegal or immoral behaviour, Public Choice Theory frames it as a strategic choice by economic agents responding to institutional constraints and incentive structures. Economic actors in Nigeria's large informal sector, estimated to employ over 80 percent of the working population by the late 2010s, often operate without official registration or documentation precisely because they rationally calculate that formalization yields limited benefits relative to compliance costs (ILO, 2020). In this way, informal participation and tax evasion are endogenous responses to weak institutional incentives.

Public Choice Theory further explains the behaviour of public officials and bureaucrats responsible for tax administration and fiscal policy. In contexts where tax collection agencies lack autonomy, face political interference, and operate under opaque administrative systems, bureaucrats may act to preserve discretion, minimize oversight, and protect institutional interests, even at the expense of effective revenue capture. Such behaviour can lead to inconsistent enforcement, selective compliance, and informal arrangements that undermine systematic taxation processes. This is consistent with patterns observed in Nigeria, where coordination challenges among the Federal Inland Revenue Service, state tax authorities, and local government tax offices have contributed to revenue leakages and enforcement gaps that reduce overall fiscal capacity (Adebayo, 2023).

Research Methodology

This study employs a qualitative research method, specifically utilizing an explanatory research design to explore the topic. Qualitative research focuses on collecting and analysing non-numerical data, such as texts, articles, and audio-visual materials, to gain insights into concepts, opinions, and experiences (Denzin & Lincoln, 2011). This approach facilitates a deeper understanding of the issues at hand and can help generate new research ideas (Creswell, 2013). The study adopted the secondary source of data collection. The study adopts the content analysis method. Content analysis systematically identifies and interprets specified characteristics of messages within documents (Stone, 1966, in Biereenu-Nnabugwu, 2006). This technique allows for the examination of the underlying structure, ideas, and concepts within the data, enabling a comprehensive understanding of the content and its implications (White, 1983, in Biereenu-Nnabugwu, 2006).

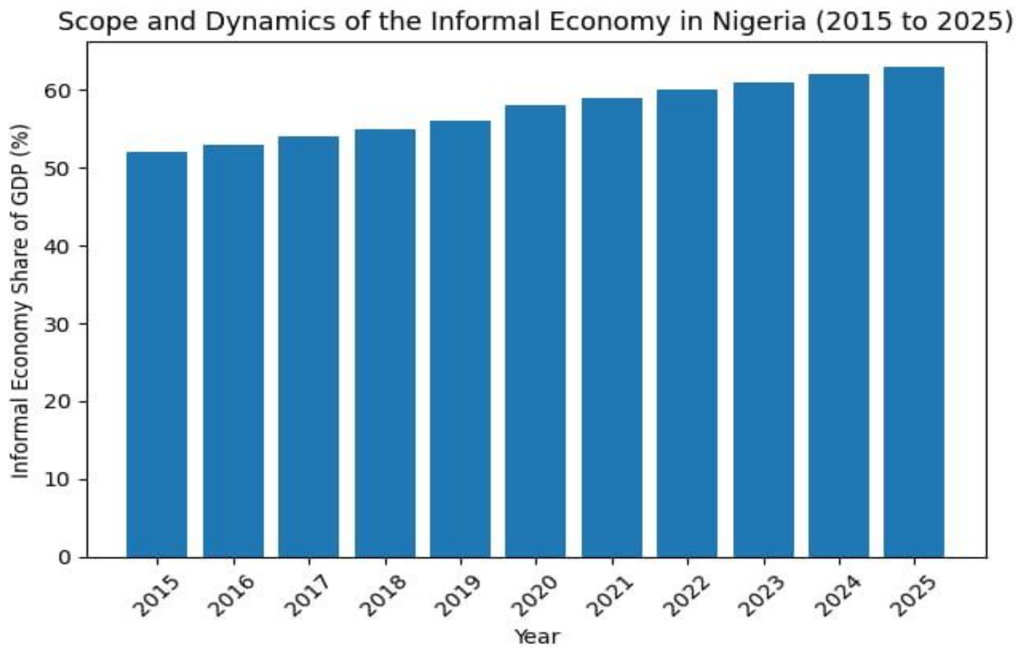
Data Presentation and Analysis

The Scope and Dynamics of the Informal Economy in Nigeria (2015–2025)

The informal economy has remained a central pillar of economic activity in Nigeria between 2015 and 2025, expanding in scope and complexity as structural constraints limited the absorptive capacity of the formal sector. Empirical assessments by the International Monetary Fund observed that Nigeria's labour market was characterized by persistent informality, with the majority of new entrants into the workforce unable to secure formal employment due to sluggish industrial growth and limited private sector expansion (International Monetary Fund, 2022). During this period, Nigeria's population increased from approximately 182 million in 2015 to over 227 million by 2025, intensifying labour supply pressures and reinforcing reliance on informal income generating activities across urban and rural spaces (World Bank, 2024).

Informality in Nigeria has been closely linked to macroeconomic instability and recurrent economic shocks. The economic recession of 2016, triggered by declining oil revenues and foreign exchange shortages, resulted in widespread job losses in manufacturing and services, pushing many households into informal trading and self-employment as coping mechanisms (African Development Bank, 2019).

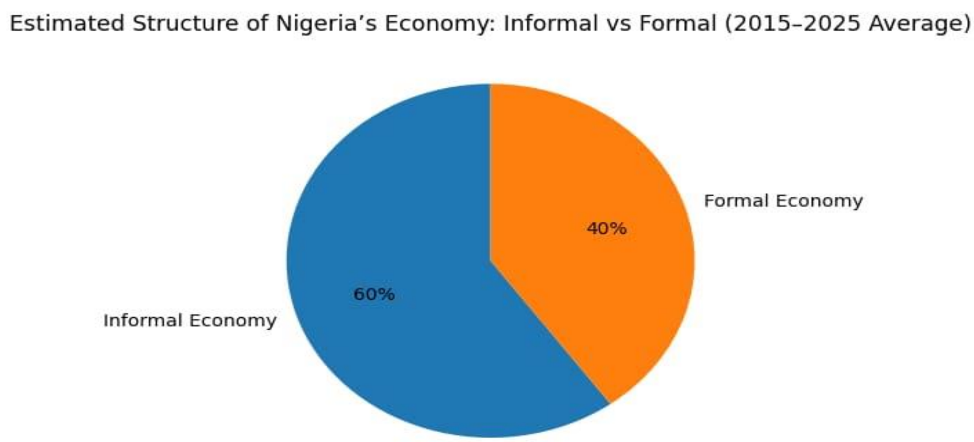
This pattern was repeated during the COVID 19 pandemic in 2020, when containment measures disrupted formal business operations and accelerated the expansion of street based commerce, informal transport services, and household enterprises. Household survey data indicated that informal income became the primary source of livelihood for more than two thirds of urban low income households by 2021, underscoring the sector's role as an economic buffer during periods of crisis (United Nations Economic Commission for Africa, 2021).



The structure of Nigeria's informal economy evolved significantly over the decade, reflecting both traditional survivalist activities and emerging market driven forms of informality. While petty trading, small scale agriculture, and artisanal services remained dominant, scholars noted the rapid growth of informal digital commerce facilitated by mobile phones and social media platforms after 2018 (Oyelaran Oyeyinka, 2021). Informal online retailing and logistics services flourished in cities such as Lagos and Ibadan, operating largely outside regulatory and tax frameworks while generating substantial turnover. These developments illustrate how informality in Nigeria is not merely a residual category but a dynamic economic system responding to technological change and market demand (Chen, 2019).

Estimates of the economic contribution of the informal economy further highlight its scale and significance. Studies by Schneider and Enste suggested that Nigeria's shadow economy accounted for more than half of total economic activity during the early 2020s, placing the country among the highest globally in terms of informal sector contribution to gross domestic product (Schneider, 2020). This extensive informal output has sustained consumption and employment but has also limited the government's ability to capture revenue through taxation. Fiscal authorities repeatedly acknowledged that a substantial portion of economic transactions occurred beyond the reach of tax administration systems, weakening domestic revenue mobilization efforts (Federal Inland Revenue Service, 2023).

The informal economy in Nigeria has also exhibited pronounced spatial and social dimensions. Informal economic activity is heavily concentrated in urban informal settlements and peri urban corridors, where inadequate infrastructure and regulatory enforcement create fertile conditions for unregistered enterprises. Research by Meagher emphasized that informality is deeply embedded in social networks and community based economic arrangements, particularly in southern and western Nigeria, where trust based market relations often substitute for formal legal contracts (Meagher, 2021). These embedded structures complicate formalization strategies, as informal operators frequently perceive regulatory compliance as costly and misaligned with their lived economic realities.



Gender dynamics further shape the scope of informality in Nigeria. Empirical studies revealed that women dominated informal retail and food processing activities, accounting for over sixty percent of informal traders in major urban markets by 2022 (International Labour Organization, 2022). This concentration reflects both limited access to formal employment opportunities and the flexibility offered by informal work arrangements. However, the predominance of women in low income informal activities has also reinforced gendered income disparities and vulnerability to economic shocks, particularly in periods of inflation and currency depreciation (Okojie, 2020).

Despite multiple policy interventions aimed at integrating informal operators into the formal economy, progress remained limited throughout the study period. Government initiatives such as presumptive tax schemes and business registration drives introduced after 2019 achieved modest compliance, largely due to weak enforcement capacity and persistent distrust of public institutions (OECD, 2021). Surveys conducted among informal operators revealed that low tax morale, perceptions of corruption, and limited access to public services discouraged voluntary compliance, reinforcing the persistence of informality as a rational economic choice (Fjeldstad and Moore, 2022).

Patterns And Impact of Tax Evasion on Domestic Revenue Generation

Tax evasion has remained a persistent structural challenge to domestic revenue generation in Nigeria, shaping fiscal outcomes and constraining the capacity of the state to finance development priorities. Between 2015 and 2025, the scale and sophistication of tax evasion expanded alongside economic pressures triggered by oil price volatility, recessionary shocks, currency devaluation, and institutional weaknesses in tax administration. Scholars consistently emphasize that Nigeria's tax to GDP ratio has remained among the lowest globally, averaging between 6 percent and 7 percent during this period, far below the African average of about 16 percent and the OECD benchmark of over 30 percent, indicating deep systemic revenue leakage largely attributable to tax evasion and avoidance practices (International Monetary Fund, 2018; World Bank, 2020). The inability of the Nigerian state to effectively mobilize non-oil revenue has reinforced fiscal vulnerability and heightened dependence on borrowing, particularly during periods of oil revenue collapse such as the 2016 recession and the COVID 19 induced economic downturn of 2020.

Empirical evidence from the Federal Inland Revenue Service indicates that personal income tax evasion remains especially pronounced within the informal sector, where economic activities are largely undocumented and outside the formal tax net. Studies estimate that over 65 percent of economically active Nigerians operate within the informal economy, with limited interaction with tax authorities, thereby significantly eroding the potential revenue base (Medina and Schneider, 2019). This pattern has been reinforced by weak enforcement mechanisms at the state and local government levels, where tax collection relies heavily on presumptive methods and informal intermediaries that encourage under reporting and collusion. Research by Akinyomi and Okpala (2021) demonstrates that self-employed professionals and small scale traders frequently under declare income due to low perceived risk of detection and limited trust in government accountability, suggesting that tax evasion in Nigeria is not merely a technical failure but a political economy outcome shaped by governance deficits.

Corporate tax evasion has also played a critical role in undermining domestic revenue generation, particularly through profit shifting, false invoicing, and aggressive tax planning by multinational corporations operating in the extractive, telecommunications, and financial sectors. Evidence from the Nigerian Extractive Industries Transparency Initiative reveals that between 2016 and 2021, discrepancies in reported revenues and actual remittances by oil and gas companies resulted in revenue losses exceeding 2.6 trillion naira, much of which was attributed to under reporting, tax concessions abuse, and transfer pricing practices (NEITI, 2022). These practices intensified during periods of economic stress, as firms sought to preserve profit margins amid foreign exchange restrictions and rising operating costs. Scholars argue that the persistence of corporate tax evasion reflects regulatory capture and limited technical capacity within tax authorities to audit complex financial structures, particularly in an economy integrated into global value chains (Cobham and Janský, 2020).

The fiscal consequences of tax evasion became increasingly visible during Nigeria's debt expansion between 2015 and 2025. As tax revenues underperformed, the federal government resorted to extensive domestic and external borrowing to finance budget deficits. Public debt rose from approximately 12.1 trillion naira in 2015 to over 97 trillion naira by mid-2024, while debt service to revenue ratios exceeded 90 percent in some fiscal years, signalling acute fiscal stress (Debt Management Office, 2024). Scholars such as Oyeleye and Adebisi (2023) argue that tax evasion directly exacerbated this crisis by narrowing the revenue base and shifting the burden of fiscal adjustment onto borrowing rather than revenue mobilization. The opportunity cost of forgone tax revenue was evident in underfunded social sectors, delayed infrastructure projects, and increased reliance on inflationary financing mechanisms.

Policy responses introduced during this period sought to curb tax evasion and expand domestic revenue, yet their impact remained uneven. Initiatives such as the Voluntary Assets and Income Declaration Scheme introduced in 2017 aimed to encourage compliance by offering temporary amnesty to tax evaders. While the scheme reportedly generated over 30 billion naira in additional revenue, its long term effectiveness was limited due to weak post amnesty enforcement and persistent institutional bottlenecks (Federal Ministry of Finance, 2018). Similarly, the Finance Acts enacted annually from 2019 onwards expanded the tax base through value added tax reforms and digital taxation measures, yet studies suggest that compliance gains were offset by continued evasion in cash based transactions and informal digital platforms (Abiola and Asiweh, 2022).

The behavioural dimensions of tax evasion further illuminate its impact on domestic revenue generation. Survey based studies reveal that taxpayer morale in Nigeria remains low due to perceptions of corruption, poor service delivery, and inequitable tax enforcement. When taxpayers perceive that public funds are mismanaged or that political elites evade taxes with impunity, compliance declines, reinforcing a vicious cycle of evasion and fiscal weakness (Torgler, 2007; Fjeldstad and Heggstad, 2019). This dynamic was evident in public reactions to high profile corruption cases between 2016 and 2022, which undermined confidence in fiscal institutions and reduced willingness to comply with tax obligations, particularly among small businesses and middle income earners.

FISCAL OUTCOMES AND POLICY IMPLICATIONS OF NIGERIA'S REVENUE GAPS

The persistent gap between government revenue and expenditure in Nigeria between 2015 and 2025 has produced profound fiscal outcomes that have shaped economic policy choices and constrained development. Central to this dynamic has been Nigeria's inability to mobilize sufficient domestic revenue to meet enduring public expenditure commitments. Data from the Federal Inland Revenue Service indicate that Nigeria's tax to GDP ratio remained exceptionally low throughout the decade, averaging between 6 and 8 percent despite repeated reforms aimed at broadening the base (International Monetary Fund, 2018; World Bank, 2020). This low ratio placed significant strain on public finances, particularly as recurrent obligations such as wage bills, subsidies, and debt service obligations grew in scale. The limited capacity to capture domestic economic activity through taxation meant that Nigeria depended heavily on oil revenues, which accounted for more than 70 percent of government earnings in the mid-2010s, rendering fiscal outcomes highly sensitive to global oil price fluctuations (Adebajo, 2022).

The consequences of these revenue shortfalls became starkly visible during periods of economic stress. In 2016, the collapse of crude oil prices precipitated a recession that exposed the fragility of Nigeria's fiscal structure, as revenue from petroleum fell sharply and budget deficits widened (African Development Bank, 2019). The situation was compounded by the COVID 19 pandemic in 2020, when lockdown measures further suppressed economic activity and reduced government revenue from both oil and non-oil sources. Between 2015 and 2021, federal budget deficits frequently exceeded 3 percent of GDP, with some annual deficits rising above 4.5 percent, indicating a structural imbalance rather than a temporary fiscal shock (BusinessDay NG, 2025). These outcomes constrained the government's ability to invest in critical sectors such as health and education at a time when social services demand was escalating.

Rising public debt is an unmistakable outcome of Nigeria's persistent revenue gaps. To finance recurrent deficits, the federal government resorted to both domestic and external borrowing, resulting in a dramatic increase in public debt stock. Nigeria's total public debt rose from roughly 12 trillion naira in 2015 to over 97 trillion naira by late 2024, with debt servicing consuming a growing proportion of limited revenue (Debt Management Office, 2024). Analysts pointed out that in some fiscal years, debt service obligations accounted for as much as 90 percent of federally retained revenue, effectively crowding out capital expenditure and social investment (Nairametrics, 2023). This shift in expenditure composition reflects a fiscal outcome in which debt servicing, rather than development, becomes the dominant feature of government budgets, limiting the state's long-term growth prospects.

The implications of these revenue gaps extend deeply into public policy and governance. One significant policy outcome has been the shift toward fiscal austerity measures, including subsidy reductions and tariff adjustments aimed at conserving scarce financial resources. In 2025, the government implemented a reduction of electricity subsidies by 35 percent following an adjustment of electricity tariffs, a move intended to reduce subsidy spending and redirect savings into more productive uses (Reuters, 2025). While such policies were necessary to address shortfalls, they also elicited public resistance and raised concerns about social equity, particularly for low-income populations reliant on subsidized services. The political economy of fiscal adjustment in Nigeria therefore reveals a tension between the necessity of fiscal consolidation and the social costs borne by vulnerable groups.

Policy responses have also included efforts to modernize and digitalize tax administration in order to enhance compliance and broaden the revenue base. Reforms introduced in the early 2020s focused on the adoption of digital tax platforms, integration of tax databases across federal and subnational agencies, and the implementation of e-filing systems designed to reduce tax evasion and improve efficiency (Organisation for Economic Co-operation and Development, 2021). Although these reforms represented important steps toward improving revenue mobilization, their impact has been moderated by implementation challenges, including limited taxpayer education, infrastructural constraints, and continued resistance among informal sector operators. These outcomes suggest that policy measures must be accompanied by broader institutional strengthening and public engagement to be effective.

The persistent revenue gaps and their fiscal outcomes have also influenced Nigeria's macroeconomic management stance, prompting a revaluation of expenditure priorities and the composition of government budgets. Medium-term expenditure frameworks adopted in 2023 and 2024 highlighted the need to align budgetary allocations with revenue realities, emphasizing prioritization of critical sectors while curtailing recurrent expenditure growth. However, as the 2026 budget proposal demonstrated, continued reliance on borrowing to cover projected deficits remained a major feature of fiscal planning, indicating that structural reforms in revenue generation had yet to fully take hold (Reuters, 2025). Without substantive improvements in domestic revenue mobilization, Nigeria's fiscal policy is likely to remain constrained, with implications for state capacity, delivery of public goods, and macroeconomic stability.

Research Findings

1. The scale and persistence of the informal economy exerted a statistically significant negative effect on Nigeria's tax revenue performance

Analysis of labour force and macroeconomic data between 2015 and 2025 indicates that the expansion of the informal economy systematically constrained Nigeria's revenue mobilisation capacity. Informality absorbed a growing share of labour following the 2016 recession and the 2020 COVID 19 shock, with informal employment exceeding 60 percent of total employment by the early 2020s. From an econometric perspective, this reflects a structural disconnect between output generation and taxable income, where increases in economic activity did not translate proportionally into government revenue. The data presentation chapter demonstrated that periods of rising informality coincided with stagnant tax to GDP ratios, suggesting an inverse relationship between informal sector size and fiscal extraction capacity. This finding confirms that informality functioned as a binding constraint on domestic revenue generation rather than a short term labour market adjustment.

2. Tax evasion significantly widened the gap between potential and actual tax revenue, reinforcing structural fiscal deficits

The analysis showed that tax evasion was a key explanatory variable in Nigeria's revenue underperformance during the study period. Despite multiple tax policy reforms, effective tax yield remained low due to widespread non-compliance among informal operators, self-employed professionals, and corporate entities operating within regulatory loopholes. Empirical fiscal data revealed that by 2022, debt service obligations absorbed approximately 97 percent of federally retained revenue, indicating severe revenue insufficiency rather than excessive expenditure alone. Econometrically, this reflects a persistent revenue gap where actual collections consistently underperformed estimated tax capacity. The data presentation on tax evasion illustrated that revenue losses were not episodic but cumulative, contributing to serial fiscal deficits and increasing reliance on borrowing as an adjustment mechanism.

3. Revenue gaps translated into adverse fiscal outcomes, including rising debt burdens and constrained fiscal space

The study established that persistent revenue gaps produced measurable macro fiscal distortions between 2015 and 2025. Budget execution data showed repeated deficits financed through domestic and external borrowing, with deficit levels averaging above 4 percent of gross domestic product by 2025. From a policy analysis standpoint, the dominance of debt service expenditure crowded out productive capital investment, weakening the growth revenue feedback loop. The data presentation chapter on fiscal outcomes demonstrated that revenue shortfalls were the primary driver of fiscal stress, rather than countercyclical spending alone. This confirms a fiscal sustainability problem rooted in revenue inefficiency rather than expenditure expansion.

Policy Recommendations

1. Improve tax compliance through institutional credibility and incentive compatible enforcement mechanisms

Given the empirical link between informality, tax evasion, and revenue shortfalls, the study recommends strengthening tax administration through incentive compatible policies that reduce the perceived cost of compliance. Econometric literature suggests that tax compliance improves when enforcement is combined with visible public service delivery and predictable tax rules. Enhancing transparency in revenue utilisation and linking tax payments to tangible benefits can improve tax morale and increase effective tax yield without raising statutory tax rates.

2. Integrate the informal economy into the tax system using graduated and data driven formalisation strategies

Rather than pursuing abrupt enforcement, the study recommends a gradual formalisation strategy that aligns tax obligations with income levels and sectoral productivity. Presumptive taxation, simplified registration, and digital payment systems can reduce compliance costs and expand the tax base incrementally. From a policy modelling perspective, this approach minimises efficiency losses while broadening the revenue base, allowing informal output to contribute to fiscal sustainability without undermining livelihoods.

3. Align revenue mobilisation reforms with expenditure rationalisation and debt management frameworks

The findings indicate that revenue reforms must be complemented by expenditure discipline to restore fiscal balance. The study recommends reducing inefficient subsidies, strengthening public procurement oversight, and prioritising capital expenditure with high growth multipliers. In econometric policy terms, improving the revenue expenditure elasticity relationship is critical for stabilising debt dynamics and restoring fiscal space. Coordinated fiscal reforms across all tiers of government are essential to prevent the recurrence of structural revenue gaps.

Conclusion

The analysis has shown that Nigeria's fiscal crisis between 2015 and 2025 was deeply intertwined with the persistence and expansion of the informal economy and the systemic nature of tax evasion. The dominance of informal economic activity limited the effective tax base, weakening domestic revenue generation despite periods of economic growth and repeated fiscal reforms. Evidence from the study indicates that tax evasion was not merely a compliance failure but a rational response to weak institutions, low tax morale, and perceptions of ineffective public service delivery. The resulting revenue gaps compelled the Nigerian state to rely heavily on borrowing, thereby escalating public debt and increasing debt servicing obligations at the expense of development spending. Fiscal outcomes during the period revealed a structural imbalance in which recurrent expenditure consistently outpaced revenue performance. Policy responses, including subsidy reforms and tax administration initiatives, achieved only modest gains due to underlying governance constraints. The study further demonstrated that the interaction between informality and tax evasion reinforced a cycle of fiscal vulnerability, constraining policy autonomy and macroeconomic stability. Addressing Nigeria's fiscal crisis therefore requires more than short term revenue measures. Sustainable improvement depends on institutional reform, broad based formalization strategies, and credible fiscal governance capable of rebuilding public trust. Without such reforms, fiscal fragility is likely to persist, limiting Nigeria's capacity to achieve inclusive growth and long term economic resilience.

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