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Article

Mechanisms of the Impact of Tax Incentives on Household Income Growth (Empirical Analysis)

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Abstract: The main purpose of this study is to examine the role of tax incentives as a fiscal instrument in increasing real household incomes under inflationary conditions and to identify effective mechanisms through which tax incentives influence income growth. Using the case of Uzbekistan, the study aims to assess how tax incentives interact with household income dynamics, domestic demand, and macroeconomic stability, as well as to develop evidence-based policy recommendations. The research employs a mixed-method approach combining theoretical analysis and simplified empirical assessment. The study is based on official statistical data from the State Statistics Agency of the Republic of Uzbekistan and the Ministry of Economy and Finance for the period 2019–2024. Comparative analysis, logical analysis, and systemic approaches are used to examine the structure of household incomes and tax incentives. Empirical assessment is conducted through the analysis of growth rates of nominal and real household incomes, consumer price index (CPI), and tax incentives, as well as ratio-based comparisons to identify relationships among these indicators. The results indicate that tax incentives have played a significant role in supporting the growth of real household incomes in Uzbekistan. Periods characterized by higher growth rates of tax incentives were associated with substantially stronger real income growth. The findings also show that tax incentives did not lead to a sharp acceleration of inflation, suggesting their effectiveness as a stabilizing fiscal tool.

Keywords: Tax Incentives, Household Income, Real Income, Consumer Price Index, Inflation, Fiscal Policy, Income Dynamics, Tax Burden, Empirical Analysis.

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1. Introduction

Sustained growth in household incomes is a key factor in expanding domestic demand and ensuring economic stability. In the context of increasing inflationary pressures, tax incentives are gaining particular importance as an effective fiscal instrument for preserving and increasing real household incomes. Therefore, the empirical examination of the mechanisms through which tax incentives affect household incomes, as well as their improvement, constitutes a pressing scientific and practical task at the present stage. According to experts, tax incentives play an important fiscal role in stimulating economic activity and supporting various categories of taxpayers by reducing the tax burden [1].

As emphasized by the President of the Republic of Uzbekistan, Sh. M. Mirziyoyev, it is possible to satisfy the population by increasing household incomes while simultaneously reducing the tax burden. The economic strategy of the "New Uzbekistan" sets the goal of achieving sustainable economic growth by 2030 and joining the group of

upper-middle-income countries, increasing the incomes of 4.5 million people at risk of falling into poverty, ensuring productive employment for the population, and raising per capita income to USD 4,000 as key priorities [2].

This article aims to examine the mechanisms for increasing household incomes through tax incentives and to develop practically significant recommendations based on empirical analysis in this area. Increasing real household incomes, expanding domestic demand, and ensuring economic stability are among the priority directions of state economic policy in Uzbekistan. From this perspective, improving the tax incentive system is of great importance for the country's socio-economic development. In this context, the formation of effective mechanisms that enhance real household incomes and stimulate economic activity through tax incentives emerges as a particularly urgent task.

2. Methodology

In the course of the study, general and specific methods of cognition were applied, including empirical analysis, analysis and synthesis, induction and deduction, a systemic approach, logical analysis, as well as methods for substantiating scientific conclusions.

Literature review

In the economic literature, the concept of "tax incentives" has not been sufficiently systematized, and existing studies primarily focus on their forms of application rather than their conceptual essence. In this regard, this article considers it necessary to clarify the economic nature of tax incentives and to provide a scientific justification of their impact on household income.

The Russian economist Panskov V. G., in his article *"Some Theoretical Aspects of the Concept of Tax Incentives"*, defines tax incentives as a method of taxation applied to subjects with a limited ability to pay taxes within the framework of the theory of tax justice, emphasizing their role in ensuring equity in the tax system [3].

Klemm A. and Van Parys, in their International Monetary Fund working paper *"Empirical Evidence on the Effects of Tax Incentives"*, define tax incentives as tax provisions that contradict the generally accepted principles of tax neutrality and fairness, as they are aimed at stimulating both foreign and domestic investment [4].

According to the explanatory dictionary by D. N. Ushakov, the term "stimulus" (from the Latin *stimulus*, literally meaning a pointed stick) refers to a factor that encourages activity by creating favorable conditions for development [5].

Uzbek economists A. Juraev and others consider tax incentives to be various forms of tax relief granted to taxpayers, which may be temporary or permanent, full or partial, and implemented in different forms depending on policy objectives [6].

The founder of Keynesian economic theory, J. M. Keynes, emphasized that reductions in taxation lead to increases in net profits of enterprises, higher investment activity, and lower unemployment, and also highlighted the potential of tax incentives as a tool for stimulating economic development [7]. However, a limitation of this approach lies in the risk that excessive state support through tax incentives may contribute to economic distortions, lead to fiscal imbalances, and reduce market competition.

Z. Kurbanov and F. Akramov, in order to clarify the essence of tax incentives, theoretically classify them into three main groups:

– full or partial exemption from taxes;

– tax deductions;

– tax credits (long-term deferral of tax and mandatory payment obligations) [8].

In our view, tax incentives should be defined as advantages stipulated in tax legislation for certain categories of taxpayers in comparison with other taxpayers, including the possibility of full or partial exemption from taxes or the payment of taxes in

reduced amounts. Furthermore, we consider it appropriate that the accounting of tax incentives be carried out by tax authorities through the use of information systems, with the assignment of a specific identification code to each type of tax incentive.

3. Result and Discussion

The conducted theoretical analysis indicates that there is a lack of comprehensive and systematic scientific research devoted to explaining the mechanisms through which tax incentives influence the growth of household incomes. Existing studies mainly focus on specific types of tax incentives and their fiscal or social consequences, while the integral aspects of the mechanisms through which tax incentives affect incomes have not been sufficiently explored.

In the economic literature, household income is interpreted as a complex economic category formed from multiple sources. According to international economic approaches, the structure of individual income includes income from labor activity (wages and equivalent payments), income from entrepreneurship and self-employment, income from property (rental income, interest, and dividends), as well as transfer payments [9]. These income sources represent key factors determining the level of economic activity and consumption capacity of the population.

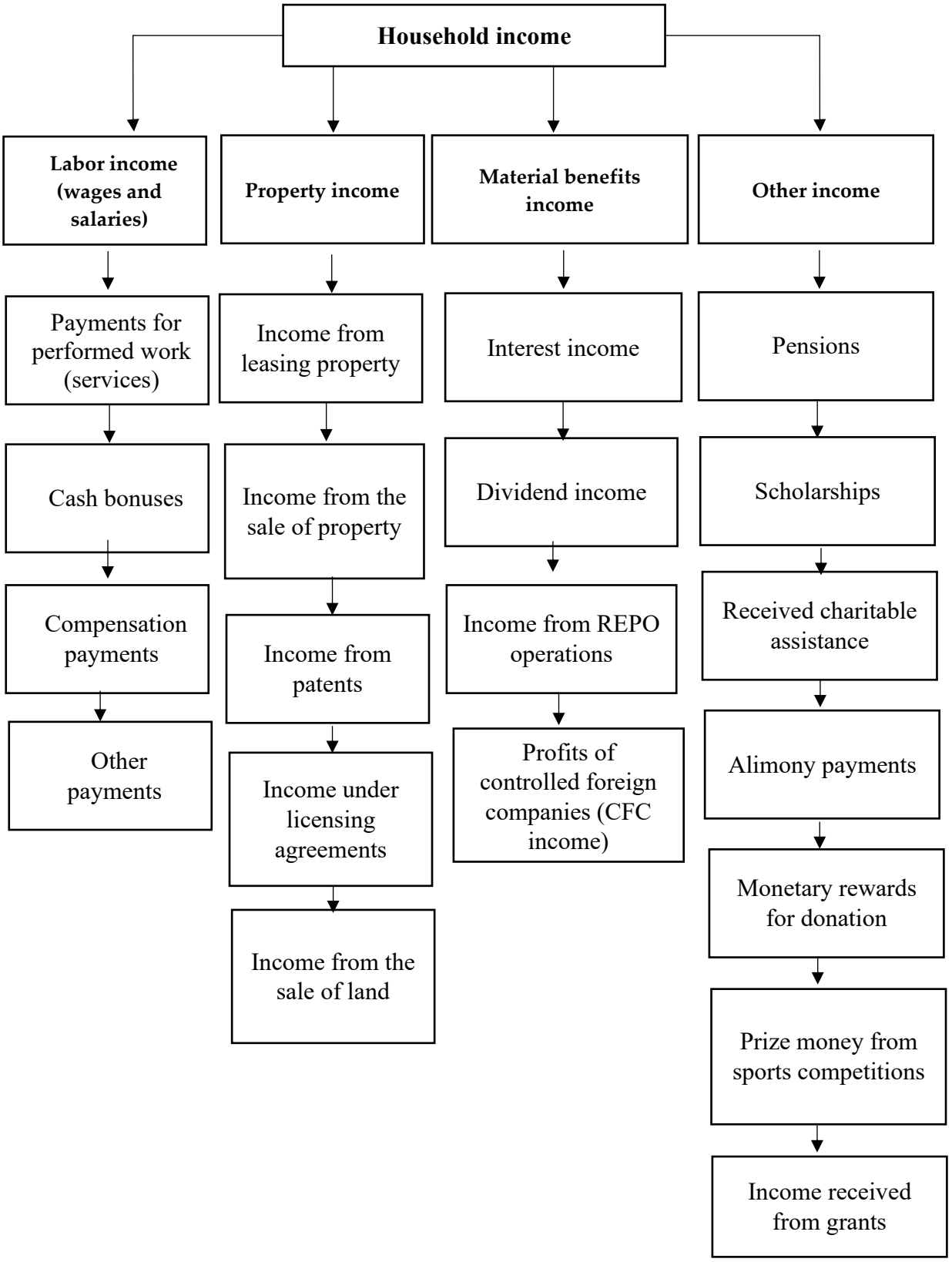

Figure 1. Structure of Total Household Income.

Developed based on the author's research.

In accordance with the current tax legislation of the Republic of Uzbekistan, total household income is classified into income from employment, property income, income in the form of material benefits, and other types of income (Figure 1). This classification not

only identifies the sources of income formation but also enables the regulation of the tax burden applied to them. From this perspective, tax incentives are applied in a differentiated manner across specific income categories, thereby increasing the amount of real income retained by households. Consequently, an in-depth analysis of the structure of household income makes it possible to identify which income sources allow tax incentives to exert a stronger impact on household incomes. This provides an important theoretical basis for empirically assessing the mechanisms of tax incentives and improving them with a focus on increasing household incomes.

Household income generally consists of several main components, among which labor income (wages and salaries) accounts for the largest share[10,11]. Economic studies indicate that wages and salaries constitute approximately 60% of personal income, highlighting their role as the primary source of income. Income derived from property (such as rental income, interest on assets, and dividends) is also included in the structure of personal income; however, its share is typically significantly lower than that of labor income and usually amounts to only a few percentage points. For example, rental income may account for 2–3% of personal income, interest income for 10–13%, and dividend income for 2–4%. Income from entrepreneurship and self-employment (proprietor's income) also plays an important role in personal income formation, often accounting for around 10% of total income. Social transfer payments (including pensions, social benefits, and unemployment assistance) frequently represent approximately 15–20% of total personal income, particularly in developed economies where social protection systems are more extensive [12,13]. Therefore, wages and salaries represent the most significant component of personal income and play a central role in determining household purchasing power and domestic demand.

In international practice, tax incentives are most effectively applied to labor income (for example, through tax refunds or reductions in tax rates) as a means of increasing real household incomes and stimulating consumption. In addition, tax incentives related to transfer income (such as child tax credits and tax relief linked to social assistance) strengthen social support for low-income households and help stabilize aggregate consumption. The introduction of tax incentives for families with children, pensioners, and low-income groups contributes to higher real incomes and stimulates their socio-economic activity, thereby promoting macroeconomic stability and growth in purchasing power.

In this context, it is essential to systematically classify tax incentives applied to income categories that occupy a dominant position in the structure of household income and to clarify their economic content. Tax incentives are applied in a differentiated manner depending on income sources, and their mechanisms of impact on real income vary accordingly. The system of tax incentives influencing household income encompasses complex and multifaceted economic relationships, and their effective implementation requires the formation of a multi-element economic mechanism aimed at increasing incomes[14]. The tax incentive mechanism proposed in this study differs from existing practices in that, based on a comprehensive classification of tax incentive types, certain elements of the mechanism have been revised and improved to enhance the effectiveness of their impact on income. Accordingly, the following section provides a detailed discussion of the main types of tax incentives that contribute to increasing household incomes and their practical significance (Figure 2).

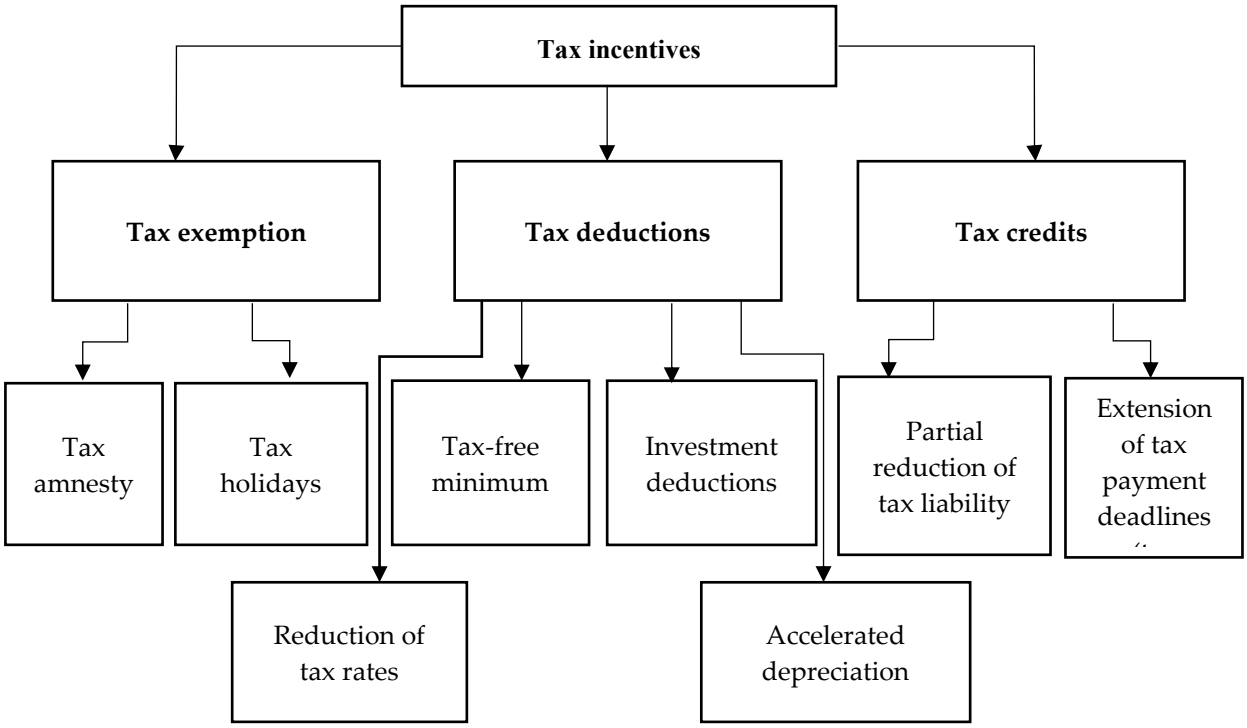

Figure 2. Classification of Tax Incentives by Groups [15].

Developed based on the author's research.

Figure 2. above presents a classification of tax incentives grouped according to their economic content and application mechanisms, which makes it possible to identify the channels through which tax incentives affect household incomes. In particular, tax exemptions increase the amount of net income retained by households by excluding a certain portion of income from the tax base.

Measures such as tax amnesties and tax holidays reduce the financial burden in the short term and have a positive effect on income stabilization. The mechanism of tax deductions, by contrast, aims to increase real income through tax-free thresholds and investment-related deductions, and its impact is relatively long-term in nature. In particular, reductions in tax rates stimulate labor participation and contribute to an increase in the share of formally declared incomes.

Accelerated depreciation affects household incomes indirectly by supporting income associated with investment and entrepreneurial activity. Tax incentives in the form of tax credits enhance current liquidity by temporarily reducing tax liabilities or extending payment deadlines. Such mechanisms are especially important for low- and middle-income groups.

Overall, the tax incentives presented in the figure function as mechanisms that exert both direct and indirect effects on household income growth. Therefore, the targeted application of these incentives in line with specific income categories represents an important economic instrument for increasing real household incomes and stimulating consumption activity.

Based on the theoretical approaches discussed above, the next stage of the study empirically assesses the impact of tax incentives on household incomes using the case of the Republic of Uzbekistan. In this stage, the relationships between nominal and real household incomes, the consumer price index, and the volume of tax incentives granted to individuals and legal entities are analyzed. These relationships are identified using correlation and regression methods while taking inflationary factors into account.

Table 1. Growth Rates of Nominal and Real Household Incomes, Consumer Price Index, and Tax Incentives in the Republic of Uzbekistan (2019–2024).

№	Indicators	Years					
		2019	2020	2021	2022	2023	2024
1	Growth rate of nominal household income, % (+,-)	+21.6	+13.1	+24.9	+21.6	+15.4	+18.5
2	Growth rate of real household income, %	+6.2	+0.1	+12.7	+9.2	+5.0	+8.1
3	Consumer Price Index (CPI), %	+14.5	+12.9	+10.0	+12.3	+8.8	+9.8
4	Growth rate of granted tax incentives, %	+28.3	+6.6	+39.9	+59.0	-5.0	+3.1

Developed by the author based on data from the State Statistics Agency of the Republic of Uzbekistan [11] and the Ministry of Economy and Finance [12]

Based on data for the period 2019–2024, the relationship between tax incentives, real household incomes, and the consumer price index (CPI) was assessed using simplified empirical methods. At the initial stage, the average annual growth rates of the main indicators over the analyzed period were calculated [13]:

$$\overline{RHI} = \frac{6.2 + 0.1 + 12.7 + 9.2 + 5.0 + 8.1}{6} \approx 6.9\%$$

$$\overline{CPI} = \frac{14.5 + 12.9 + 10.0 + 12.3 + 8.8 + 9.8}{6} \approx 11.4\%$$

$$\overline{TI} = \frac{28.3 + 6.6 + 39.9 + 59.0 - 5.0 + 3.1}{6} \approx 21.9\%$$

These results indicate that during the analyzed period, the average growth rate of tax incentives was significantly higher than the growth rate of real household incomes, suggesting that tax incentives were actively applied as a factor supporting real income growth.

Analysis of income and investment data obtained from the studies revealed a direct relationship with high statistical significance between investment, consumption and taxes [14].

To further identify the impact mechanisms of the key variables, the dynamics of real household incomes were compared between years in which tax incentives increased and those in which they declined. In particular, during the years characterized by a sharp increase in tax incentives (2021–2022), the average growth rate of real household incomes amounted to:

$$\overline{RHI}_{TI\uparrow} = \frac{12.7 + 9.2}{2} \approx 11.0\%$$

By contrast, in the years characterized by low or negative changes in tax incentives (2020 and 2023–2024), the average growth rate of real household incomes was:

$$\overline{RHI}_{TI\downarrow} = \frac{0.1 + 5.0 + 8.1}{3} \approx 4.4\%$$

This simple comparison demonstrates that during periods of higher tax incentives, the growth of real household incomes was nearly 2.5 times greater.

The difference between the consumer price index and real household incomes was assessed using the following simple ratio:

$$\text{Difference} = RHI - CPI$$

For example, in 2021, this difference was:

12.7−10.0=+2.7 **percentage points**

This finding confirms a significant increase in real household incomes under conditions of relatively low inflation. By contrast, in 2020, when the consumer price index was high, real household incomes showed almost no growth.

The effect of a one-unit increase in tax incentives can be assessed using the following simplified ratio:

$$\text{Effect} = \frac{\overline{RHI}}{\overline{TI}} = \frac{6.9}{21.9} \approx 0.3$$

This result implies that a one percentage point increase in the growth rate of tax incentives led, on average, to a 0.3 percentage point increase in the growth rate of real household incomes. At the same time, the average growth of the consumer price index was significantly lower than the growth of tax incentives, indicating that tax incentives do not act as a factor that sharply accelerates inflation.

4. Conlusion

In conclusion, the results of the conducted theoretical and simplified empirical analysis indicate that, under the conditions of Uzbekistan, tax incentives represent an important fiscal instrument for increasing real household incomes. In our view, the growth of tax incentives supported the dynamics of real incomes without significantly intensifying inflationary pressure. This confirms that tax incentives function as an effective economic mechanism for ensuring a stable increase in household incomes and expanding domestic demand.

Based on the conclusions presented above, it is considered appropriate to propose the following policy recommendations aimed at enhancing the role of tax incentives in increasing household incomes:

- Expanding the orientation of tax incentives toward wage income, since wages constitute the largest share in the structure of household incomes, and incentives in this area yield the highest effectiveness in increasing real incomes.
- Introducing targeted tax incentives for low- and middle-income groups, which would contribute to stabilizing the real incomes of families with children, pensioners, and socially vulnerable population groups.

- Strengthening the mechanism for evaluating the effectiveness of tax incentives, including regular monitoring of their impact on real incomes and consumption levels, with the aim of reducing inefficient incentives and further developing effective instruments.
- Aligning tax incentives with inflationary processes, as tax incentives aimed at protecting incomes during periods of heightened inflationary pressure play a crucial role in preserving household purchasing power.

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