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AN INTEGRATIVE MODEL OF TAX INCENTIVES AND FINANCIAL LITERACY FOR THE PERFORMANCE OF TASIKMALAYA MSME

[1)]Bambang Kurnia Nugraha *, [2)]Hendi Sobari
[1,2]*Management Study Program,* Sekolah Tinggi Ilmu Ekonomi Latifah Mubarokiyah
Coresponding Author : *bambang300687@gmail.com*

ABSTRACT

This article develops an original model on the effect of tax incentives on the financial performance of MSMEs by adding financial literacy as a moderating variable. The development was carried out through a conceptual synthesis of research on 100 MSMEs in Tasikmalaya Regency and empirical literature on financial literacy. The results of the baseline study indicate that tax incentives have a positive and significant effect on financial performance, with a regression coefficient of 0.907, a t-value of 17.1897, and an R^2 of 0.654. The literature synthesis indicates that financial knowledge, skills, attitudes, and behaviors help MSME owners translate tax savings into more effective working capital, record-keeping, cost control, and investment decisions. The revised model allows financial literacy as a strengthening factor in the relationship between tax incentives and financial performance. This article does not report moderation coefficients because the initial research instrument did not measure financial literacy; the model was prepared as a follow-up empirical design that differs from the original study.

Keywords: tax incentives; financial literacy; financial performance; MSME; fiscal policy; moderation model.

INTRODUCTION

Micro, Small, and Medium Enterprises (MSMEs) play a strategic role in workforce absorption, income distribution, and strengthening the regional economy. Research sources note that Tasikmalaya Regency had 46,883 MSMEs in 2024, spread across 39 sub-districts, operating in the trade, culinary, crafts, agribusiness, creative industries, and services sectors. This growth reflects significant economic potential, but does not automatically translate into increased revenue, profits, liquidity, and business continuity (Khoirurrosidin, 2026).

One government instrument to assist MSMEs is tax incentives. These policies can include tariff reductions, certain obligations, administrative relaxation, and reporting simplification. Economically, reducing the tax burden should retain more cash within the business. Funds not spent on taxes can be used for inventory, operational costs, strengthening working capital, or productive investments. Therefore, tax incentives can be viewed as an external resource with the potential to improve the financial condition of MSMEs (Taxation Supervisory Committee, 2022; Hidayat, Septiyana & Monaliza, 2025).

However, the benefits of fiscal policy are not solely determined by the availability of facilities. Preliminary research indicates that MSMEs' attitudes toward tax incentives and financial performance are both in the poor category, although the relationship between the two is positive and significant. This finding suggests a gap between the potential of the policy and the ability of businesses to utilize it. Limited information, unequal understanding of procedures, and weak financial record-keeping can prevent tax savings from being translated into productive business decisions (Ainiyah, 2025; Khoirurrosidin, 2026).

In this context, financial literacy becomes a relevant variable. The OECD (2020) defines MSME financial literacy as a combination of awareness, knowledge, skills, attitudes, and behaviors that help business owners make informed financial decisions. MSME owners who understand cash flow, costs, debt, risk, and planning can more easily identify the economic value of tax incentives. Conversely, business owners with low literacy may receive tax breaks but fail to save them, mix personal and business funds, or allocate funds to activities that do not support performance.

Empirical research has demonstrated a positive relationship between financial literacy and MSME performance. Agyapong and Attram (2019) found that owner-manager financial literacy is positively associated with financial performance. In the Indonesian context, Mihardjo and Ningtyas (2023) demonstrated that financial literacy has a positive and significant effect on the financial performance of MSMEs in Bandung. Kulathunga et al. (2020) also explained that financial literacy supports performance through corporate risk management practices. This evidence provides a basis for positioning financial literacy not only as a direct predictor but also as a capability that determines the strength or weakness of tax incentive benefits.

This article refines and differentiates the original research model by adding financial literacy as a moderating variable. The objectives are: first, to restate basic empirical evidence regarding the effect of tax incentives on financial performance; second, to explain the direct influence of financial literacy on MSME performance; and third, to outline how financial literacy can strengthen the relationship between tax incentives and financial performance. Thus, the article's contribution shifts from a single-predictor model to an integrative model of fiscal policy and the internal capabilities of business actors.

LITERATURE REVIEW

Tax Incentives as a Fiscal Resource

Tax incentives are special treatment that reduces the tax burden or costs of achieving specific economic goals. For MSMEs, the immediate benefit is increased funds that can be retained for business activities. These savings have the potential to improve liquidity, reduce cost pressures, and increase the efficiency of working capital management. Agustiana, Nuridah, and Sagitarius (2023) show that tax incentives affect MSME welfare, while Ainiyah (2025) emphasizes the benefits of administration and efficiency, although their utilization is still hampered by socialization.

From a fiscal policy perspective, tax reductions will be effective if they encourage productive activity. At the company level, the mechanism is not simply a reduction in taxes, but rather a change in decision-making capacity. MSMEs can maintain inventory, make timely payments, reduce reliance on short-term debt, or introduce simple innovations. Therefore, the policy's impact needs to be assessed through financial outcomes and how businesses manage the fiscal space gained.

Financial Literacy of MSME Owners

Financial literacy is a broader skill than knowledge of financial terms. The OECD (2020) measures it through the financial knowledge, behaviors, and attitudes of MSME owners. Knowledge includes understanding interest, inflation, risk, financing, and financial reporting. Behaviors include recording transactions, planning, separating personal and business funds, and evaluating cash flow. Attitudes reflect prudence, a long-term orientation, and a willingness to compare alternatives before making a decision.

Financial literacy serves as human capital that enables business owners to transform information into action. Agyapong and Attram (2019) found a positive relationship between owner-manager financial literacy and SME performance. Mihardjo and Ningtyas (2023) demonstrated that the ability to understand financial concepts helps MSMEs implement business strategies and improve performance. Kulathunga et al. (2020) demonstrated that financial literacy is also related to risk management practices, enabling MSMEs to better respond to infections.

In this article's model, financial literacy plays two roles. First, it is estimated to directly impact performance by improving the quality of record-keeping, budgeting, financing, and cost control. Second, it is estimated to strengthen the influence of tax incentives because more literate business actors are able to save taxes, allocate them productively, and channel their impact onto profits and cash flow.

Financial Performance of MSMEs

Financial performance reflects a business's ability to generate revenue and profit, maintain cash flow, control costs, and sustain growth. For MSMEs with formal reporting, assessments can be based on profitability, liquidity, solvency, and sales growth. However, the research source used owner perceptions because some respondents lacked structured financial reporting. Indicators include revenue, profit, cash flow stability, ability to cover operational costs, and business losses (Khoirurrosidin, 2026).

Perceptual measurements are useful for capturing the experiences of stakeholders, but they need to be supplemented with objective data in future research. The inclusion of financial literacy in the revised model also explains why record-keeping quality matters: the better the owner's financial capabilities, the more likely it is that performance indicators can be measured consistently and used for decision-making.

Integrative Model and Hypothesis

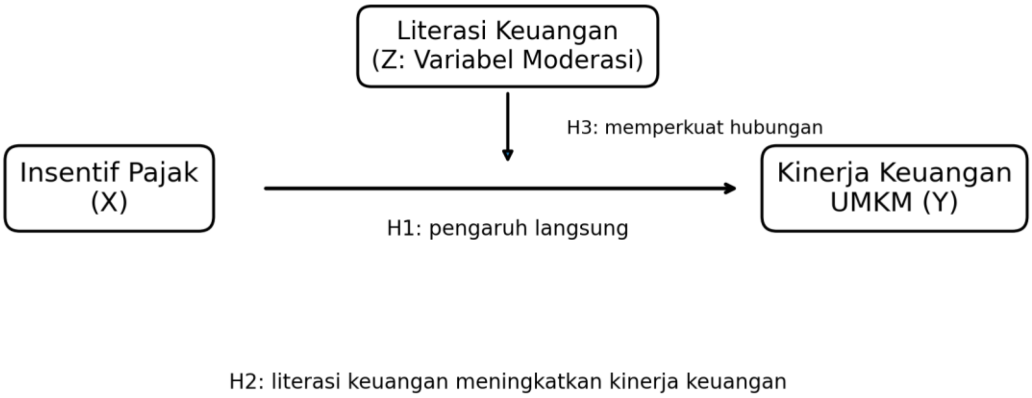
The original model only tested the direct relationship between tax incentives and financial performance. The revised model adds financial literacy as a variable with both a direct and moderating effect. Logically, tax incentives provide financial space, while financial literacy determines the quality of use of that space. The combination of external policies and internal capabilities is expected to produce stronger performance than either factor alone.

Table 1. Differences between the original research model and the revised model

Aspect	Original Model	Model Revision
Variables	Tax incentives (X) and financial performance (Y)	Tax incentives (X), financial literacy (Z), and financial performance (Y)
Connection	Direct effect of X → Y	Direct influence X → Y; Z → Y; moderation X × Z → Y
Analysis	Simple linear regression	Moderated regression/hierarchical regression or PLS-SEM

The hypotheses developed are: H1, tax incentives have a positive effect on the financial performance of MSMEs; H2, financial literacy has a positive effect on the financial performance of MSMEs; and H3, financial literacy strengthens the positive influence of tax incentives on the financial performance of MSMEs.

Figure 1. Conceptual model of revised research



Source: selection from Khoirurrosidin (2026), OECD (2020), and Mihardjo & Ningtyas (2023).

METHOD

This article uses an evidence-based conceptual model development design. The primary materials are the research report by Khoirurrosidin (2026) and the STRAMER article developed from it. The basic research employed an associative quantitative approach to 100 MSMEs in Tasikmalaya Regency. Data were collected through a Likert-scale questionnaire and analyzed using validity and reliability tests, descriptive statistics, classical assumption checks, simple linear regression, t-tests, and coefficients of determination.

To differentiate the articles from the original model, a narrative synthesis of the literature discussing financial literacy and MSME performance was conducted. The primary source for measuring additional variables was the OECD/INFE Survey Instrument for Measuring MSME Financial Literacy (OECD, 2020). Evidence of variable relationships was drawn from research by Agyapong and Attram (2019), Kulathunga et al. (2020), and Mihardjo and Ningtyas (2023), then evolved with baseline research findings.

Financial literacy is designed as a moderating variable. Further empirical testing requires the addition of questionnaire items measuring financial knowledge, behavior, and attitudes. The model can be tested using moderated regression in three stages: including tax incentives, including financial literacy, and including the interaction between tax incentives and financial literacy. Variables should be mean-centered before forming the interaction term to reduce non-essential multicollinearity. Another alternative is PLS-SEM if researchers want to simultaneously test the measurement model and structural relationships.

This article does not establish or document financial data literacy. Because the original instrument only included tax incentives and financial performance, statistical results for H2 and H3 are not yet available. The separation between empirical findings and development propositions is maintained to prevent the new model from making claims unsupported by the data.

Table 2. Revised operationalization model of variables

Variables	Role	Key indicators	Scale
Tax Incentive (X)	Independent	understanding policy; ease of administration; utilization of facilities; reduction of burden; support for business development	Likert Scale 1-5

Variables	Role	Key indicators	Scale
Financial Literacy (Z)	Moderator	Financial knowledge; Accounting and planning; cash flow management; risk attitude; decision evaluation	Likert Scale 1-5
Financial Performance (Y)	Depends	Revenue; profit; liquidity/cash flow; cost efficiency; growth and desirability	Likert Scale 1-5

Source: Variables X and Y from Khoirurrosidin (2026); variable Z adapted from OECD (2020).

RESULTS

Empirical Findings of the Basic Model

The baseline research involved 100 MSMEs, with 42% representing the 31-40 age group, followed by 37% representing the 21-30 age group. 61% of respondents were female and 39% were male. The financial performance incentive and tax instruments were declared valid and reliable. The Cronbach's Alpha for tax incentives was 0.956458 and for financial performance was 0.993681 (Khoirurrosidin, 2026).

Descriptive analysis revealed a tax incentive score of 1,851 and a financial performance score of 1,838; both of which were suggested as poor in the source article. These findings indicate that tax incentives are not yet optimally understood and utilized, while revenue, profit, and cash flow stability are not yet perceived strongly by all respondents.

Simple linear regression produces the equation $Y = 2.508 + 0.907X$. The calculated t value of 17.1897 exceeds the t table of 1.984, so the effect of tax incentives on financial performance is declared positive and significant. The coefficient of determination of 0.654 indicates that 65.4% of the variation in financial performance is explained by tax incentives in the basic model, while 34.6% is related to other factors.

Evidence Synthesis for Financial Literacy Variables

The synthesis results demonstrate the consistency of the argument that financial literacy is relevant in explaining the portion of performance variation not covered by the original model. The OECD (2020) provides a specific instrument for MSME owners that assesses the dimensions of knowledge, behavior, and attitude. Agyapong and Attram (2019) found a positive relationship between owner-manager literacy and financial performance. Kulathunga et al. (2020) showed that financial and technological literacy influence performance through risk management practices. Mihardjo and Ningtyas (2023) confirmed the positive influence of financial literacy on the financial performance of MSMEs in Bandung.

Table 3. Summary of evidence on the development of financial literacy variables

Source	Focus	Implications for the revised model
OECD (2020)	Financial literacy instruments for MSME owners	Provides standardized indicators for variable Z

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Source	Focus	Implications for the revised model
Agyapong & Attram (2019)	Owner-manager literacy and SME performance	Supports direct influence Z → Y
Kulathunga et al. (2020)	Literacy, risk management, and performance	Explaining risk management and decision mechanisms
Mihardjo & Ningtyas (2023)	Literacy and financial performance of Bandung MSMEs	Providing Indonesian contextual evidence for Z → Y

Model Development Results

The revised model yields three analytical relationships. First, the available empirical findings support H1, which states that tax incentives have a positive effect on financial performance. Second, the synthesis of previous research supports the conceptual basis of H2, which states that financial literacy has a positive effect on performance. Third, the integration of the two streams of literature yields H3, which states that financial literacy strengthens the relationship between tax incentives and financial performance.

The moderating effect is expected because competent business actors can recognize the value of tax savings, record them, and allocate them to activities that impact performance. At low literacy levels, tax incentives may only reduce liabilities temporarily without changing budgeting or working capital decisions. At high literacy levels, further savings may translate into liquidity, cost efficiencies, productive investments, and business incentives.

The coefficients for H2 and H3 cannot yet be displayed. This is not due to analytical weaknesses, but rather to the limitations of the source instrument, which does not measure financial literacy. This article concludes with one verified empirical result and two propositions ready to be tested through additional data collection.

DISCUSSION

The baseline model findings indicate that tax incentives have significant economic potential for MSMEs. A positive coefficient of 0.907 indicates that the better the understanding and utilization of incentives, the better the reported financial performance. However, the still-poor descriptive category indicates that the policy has not reached all business actors with equal effectiveness. This finding aligns with Ainiyah (2025), who identified limited socialization as the primary obstacle to utilizing tax incentives.

The addition of financial literacy addresses the explanatory weaknesses of the original model. Single-variable models tend to assume that every dollar of tax savings automatically results in improved performance. In practice, the final outcome depends on the business owner's decisions. Savings can be used to purchase productive supplies, but they can also be mixed with personal consumption. Savings can strengthen cash, but they are invisible if transactions are not recorded. Thus, financial literacy explains the process of converting policy benefits into company results.

The direct role of financial literacy is supported by empirical evidence. Agyapong and Attram (2019) showed that more literate owner-managers are able to understand financial needs and make more rational decisions. Mihardjo and Ningtyas (2023) found that literacy contributes to the financial performance of MSMEs in Bandung, making it relevant to the context of MSMEs in West Java. The findings of Kulathunga et al. (2020) further explain that literacy drives risk management practices, which is crucial when MSMEs face bottlenecks in pricing, sales, and financing.

As a moderator, financial literacy doesn't simply add another arrow to the model. This variable alters the relationship between tax incentives. Fiscal policy provides opportunities, but internal capabilities determine outcomes. Two MSMEs may receive the same facilities but achieve different outcomes due to differences in the quality of record-keeping, planning, and cash management discipline. Therefore, further research needs to examine the X×Z interaction, rather than simply including literacy as an additional predictor.

The policy implication of the revised model is the need to combine tax outreach with financial education. Simply providing information on rates and procedures is insufficient. Mentoring programs need to demonstrate how to calculate tax savings, incorporate them into cash budgets, differentiate between business and personal funds, and communicate their impact on margins and working capital. This approach encompasses exposure, fiscal facilities, and day-to-day financial decisions.

For MSMEs, the revised model emphasizes four practices. First, recording incentive benefits as savings. Second, prioritizing the use of funds for welfare, liabilities, or productive investments. Third, integrating cash flow and profits before and after receiving the incentives. Fourth, avoiding the use of tax savings for consumption that does not support the business. These practices allow the policy's benefits to be tracked and assessed objectively.

From an academic perspective, this article differs from the original research in three ways. First, the focus is no longer solely on direct impacts, but rather on the mechanisms explaining differences in benefits across business actors. Second, financial literacy is positioned as an internal capability interacting with external policies. Third, the advanced analytical method changes from simple regression to moderated regression analysis, or PLS-SEM. These differences provide clearer novelty without altering or falsifying the original research data.

Although the moderation model has a strong theoretical basis, the direction and magnitude of the effect still need to be tested. It is possible that financial literacy only has a direct effect but does not moderate the relationship. It is also possible that the incentive effect is stronger on MSMEs with medium literacy because highly literate actors already have good financial management skills before receiving incentives. Therefore, empirical testing should report the interaction coefficient, R^2 change, effect size, and simple slope graph.

CONCLUSION

This article develops a research model on tax incentives and MSME financial performance by adding financial literacy as a moderating variable. Available empirical evidence continues to indicate that tax incentives have a positive and significant effect on the financial performance of MSMEs in Tasikmalaya Regency, with a coefficient of 0.907, a calculated t of 17.1897, and an R^2 of 0.654.

Financial literacy was added because the benefits of incentives depend not only on policy but also on the business owner's ability to understand, record, and allocate taxes. The revised model proposes a direct effect of financial literacy on performance as well as a reinforcing effect on the relationship between tax incentives and financial performance. This development provides a substantive difference from the original paper and provides a more robust model for further research.

To complete the empirical paper, researchers need to add financial literacy instruments to respondents and test interactions using moderated regression or PLS-SEM. The government and tax agencies need to integrate tax education with assistance in recording, budgeting, and cash flow management so that incentives truly improve MSME performance.

LIMITATIONS

This article was developed using original research results as primary evidence and literature as a foundation for additional variables. The primary data source did not include financial literacy items, so H2 and H3 have not been statistically tested. The article does not present simulation figures or artificial moderation coefficients.

Financial performance in the initial study was measured through owner perceptions, not audited financial statements. The sample was also limited to 100 MSMEs in Tasikmalaya Regency, with a 10% sampling error. Further research should utilize targeted data, expand the sample size, control for business age, size, sector, and access to financing, and ensure robust construct validity, common method bias, and standard errors.

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