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An Evaluation of the Influence of Goods and Service Tax(GST)on Micro, Small and Medium Enterprises: Opportunities and Challenges

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Abstract

Indian MSMEs is the emerging sector over the nation and has emerged as a highly vibrant and dynamic sector of Indian Economy over the last few decades. Its participation in large employment diminishes the pressure of unemployment across the nation and this sector reduced the regional imbalances. It has found that 51 per cent of the enterprises located in rural regions and 49 per cent in the urban areas. Empirical studies have shown that MSMEs contribute over 55% of GDP and over 65% of total employment in high income countries. MSMEs and informal enterprises account for over 60 % of GDP and over 70% of the total employment in the low income countries. The MSME segment accounts for 29.7% of India's GDP and 49.66% of exports. The comprehensive GST rationalization implemented by the government targeted to achieve the objectives of flagship schemes such as Make in India, Aatmanirbhar Bharat, PM Gati Shakti, and Pradhan Mantri Awas Yojana etc. This tax reform influence directly to strengthening MSMEs, expanding job opportunities, and revitalizing local supply chains in critical sectors like automobiles, textiles, food processing, logistics, and handicrafts. Further Lower GST rates have made essential goods, raw materials, and services more affordable, motivating small and medium enterprises and start-ups to scale up operations, invest in innovation, and compete both domestically and globally. The reforms support women-led and labour-intensive industries by making manufactured goods, processed foods, apparel, and even eco-friendly products accessible at lower costs, fostering economic inclusion of rural, semi-urban, and informal sector workers alongside urban manufacturers. This study will highlight the extensive role of GST on MSME sector and also will analyze the issue of opportunities and challenges of MSMEs.

Keywords: MSMEs, regional imbalance, informal sector, supply chain

Introduction

Over the last six decades, MSME has grown as a vibrant sector of the Indian economy. It not only supports to industrialize rural and underdeveloped areas but also reduces regional disparities. This sector also creates a large number of jobs opportunities for the deprived and unskilled peoples living in underprivileged regions. Apart from it, these MSMEs function as ancillary units for big businesses and contribute considerably to the country's socio-economic progress. The Ministry of Micro, Small, and Medium Enterprises (M/o MSME) anticipates a thriving MSME sector by accelerating economic development, aiding existing businesses, and encouraging the creation of new business in association with relevant Ministries/Departments, State Governments, and other stakeholders. Empirical studies have shown that MSMEs contribute over 55% of GDP and over 65% of total employment in high income countries. MSMEs and informal enterprises account for over 60 % of GDP and over 70% of the total employment in the low income countries. Globally, this sector contributes about 70% of GDP and 95% of the total employment in the middle-income countries. The MSME segment accounts for 29.7% of India's GDP and 49.66% of exports. There are an estimated 63.4 million MSMEs employing close to 124 million people and manufacturing over 7000 products throughout the geographical expanse of India. According to the MSMEs annual report for 2020, they contribute 6% and 24% of the GDP in the manufacturing and service sector respectively. In India, both registered and unregistered MSMEs cross 63 million and contribute nearly 40 per cent of national income. It endeavours social responsibility by creating employment for over 110 million rural and underprivileged areas to eradicate regional disparities. To increase the export potential of MSMEs, Special Economic Zones and Export Promotion Zone have been created. These enterprises encourage a new breed of entrepreneurs hailing across society who have the prospects to build globally competitive enterprises. For the sustainable development of MSMEs, credit facilities are easily accessible to enterprises along with priority being given to basic infrastructure facilities, and efforts are made to develop the competency of human resources. At present the MSMEs are contributing 30 per cent of the total national income. Since1960, India's MSME sector has risen drastically, with an annual growth rate of 4.62 per cent in terms of employment (currently employing 110 million). It not only creates jobs but also helps to prevent rural-urban migration by providing a stable source of employment for those living in rural areas. In comparison with mega industries owned by big companies, these MSMEs have helped to industrialize backward areas at a minimal cost of capital. This

sector has made a significant contribution to the country's socio-economic growth as a complement to major industries.

Table- 01: Key Sectors and Industries in MSME Sector

Sectors	Allotted industries
Manufacturing	Food processing, textiles & garments (handlooms/power looms), leather products, engineering & fabrication, auto components, pharmaceuticals, and chemical manufacturing.
Service	IT solutions, hospitality & tourism (hotels/guest houses), consulting services, logistics, and Repair services (agricultural machinery, automotive)
Cottage and Village Industries	Handicrafts, bee-keeping, coir, sericulture, Khadi products, and toy manufacturing.

However Indian micro, small and medium enterprises are vital for economic growth, innovation and employment, yet they face intolerable complex tax regimes. However, GST adoption mitigates the challenges and burden to the micro and small enterprises still they face many problems and limitation from different angle of taxation. In the following table different stage of GST collection has been discussed. According to old regimes the tax structure were controlled by VAT and central excise service tax for sales with the state where new tax regime introduced CGST and SGST which do impact on revenue which to be equally transferred to both central and state government. Similarly, for the sales to another states the old tax regime was under central state tax and exercise service tax where under new regimes tax structure leaded by IGST and here central will be shared the IGST revenue based on the destination of goods.

Table-2: Different stage of GST Collection

Transaction	New regime	Old regime	Impact
Sales within state	CGST+SGST	VAT/ central exercise service tax	Revenue will be equally transferred to both central and state government
Sales to another state	IGST	Central state tax Exercise service tax	The Central will be share the IGST revenue based on the destination of goods.

Review of Literatures

A study is made by Chaithra, Murthy, and Komma (2022) and they examined the impact of GST on MSMEs in Bangalore, focusing on the Peenya Industrial Area with a sample of 110 respondents. The study found that GST has streamlined the tax structure, potentially reducing business costs and providing a uniform market for MSMEs. However, challenges related to compliance and registration persists.

Another study has made by Harishekar and Manoj (2021) and analysed the impact of GST on small-scale enterprises in Karnataka, concluding that the tax reform reduced business costs, increased transparency, and improved compliance. However, the study also identified challenges such as job work taxation, penalties for non-payment, and dual administration, which require further reforms.

Jyanthi and Selvam (2022) have formed another study where they highlighted the challenges faced by MSMEs in Bangalore regarding GST compliance. While GST has improved efficiency and reduced tax-related complexities, many businesses struggle with implementation, particularly in terms of documentation and compliance. The study suggested that government support and training programs are essential to help MSME entrepreneurs adapt to the new tax system effectively.

In another study, Pandey and Raj (2022) explored compliance issues faced by MSMEs in Karnataka, revealing that GST-related administrative burdens hinder business growth. Based on data collected from 35 MSMEs, the study emphasized the need for policy interventions to simplify compliance procedures.

On the other hand, Ajetrao (2023) assessed the awareness and impact of GST among small business owners in Mysuru. The findings shown that business owners perceive GST as a fair tax system; however, many struggle with its procedural complexities and depend on consultants for tax filings. The study suggested that increasing awareness and simplifying online submission processes could improve compliance.

Similarly, Venkateshwarlu and Vijaylakshmi (2022) made another study and examined the dual impact of GST on MSMEs, finding that while it facilitates market expansion and simplifies taxation, it also introduces new financial and administrative challenges that require adaptation.

Another study has developed by Vanishree. G & Dr. Ravindra Kumar B (Pg 1245-1255) and evaluated the regulatory implications of GST on small businesses, concluding that while GST has streamlined tax collection, it has also introduced compliance difficulties that necessitate additional support mechanisms.

Similarly, one another researcher, Pandit (2021) has made a study where he explored both the opportunities and challenges that GST presents for SMEs, noting that while the tax

reform offers a unified tax structure and broader market access, businesses must invest in technology and adapt to new financial reporting standards.

On the other hand, Kumari (2022) examined in her study the effect of GST on MSMEs in India, highlighting its potential to boost competitiveness by creating a level playing field. However, the study pointed out the initial transition difficulties, especially for small businesses unfamiliar with digital compliance systems.

Objective of the study

The main objective of this study is to analyses the proposed impact of new tax regime introduced as GST on several MSME sector in India. Enterprises are categories based on the performance in the region basis and concentrated on the issue of proposed impact of GST on these growing and effective enterprises and as well as to observe the regional imbalances.

Methodology

The study is made based on the secondary information mining from secondary sources and from the ministry of micro, small and medium enterprises. The different growing enterprises has categorized according to the effectiveness and importance in revenue creation and employment generation across the regions. Besides the enterprises has segregated on the basis of new tax reform imposed based on necessary and luxury goods. In this study GST reform variation has been calculated to illustrate the redemption of tax burden especially on micro and small enterprises performing in rural and deprive sector in India. Charts and diagrams are used to fulfill the study and to analyses the impact of new tax regime.

Analysis and discussion

The share of enterprises working under MSMEs in rural areas is a little larger than urban areas. But in case of employment the share of urban MSMEs is little more than rural MSMEs. The MSMEs reduced the regional imbalances as these production units working as informal sector in all regions across the nation. The given data shows the rural-urban divide of MSMEs working in number and employment in India. The corresponding diagram visualized the importance of micro, small and medium enterprises working in different sectors.

Tabbe-3: Number of Enterprises and Employment level in MSMEs in India (Rural-Urban Divide)

Sector	Enterprises in lakh	Share in percentage	Employment in Lakh	Share in percentage
Rural	324.88	51.2	497.78	44.8
Urban	309	48.8	612.10	55.2
Total	633.88	100	1109.89	100

Resource: Annual Report 2022-23, Ministry of Micro, Small and Medium Enterprises, GoI.

Diagram-1: Number of Enterprises and Employment level in MSMEs in India (Rural-Urban Divide)

In this table we are intended to know the new tax reform variation for automobiles industries. However these are all big industries but new GST regime do affect the society significantly. It has found that keeping GST burden unchanged for large car industries the other automobiles are comes under new GST regime where tax has reduced drastically and no doubt its impact will push economy positively. The new GST structure will be more visible if we see the following diagram.

Table-04: GST Reduction in Automobile Industries

Categories	Old GST in percent	New GST in percent	Reform Variation
Two wheeler (up to 350 cc)	28	18	10
Small cars	28	18	10
Large cars	40	40	00
Auto components	28	18	10
Tractors	12	05	08
Road tractors for semi-tractors	28	18	10
Commercial goods vehicles	28	18	10

Source: Ministry of Micro, Small and Medium Enterprises, 2025

Diagram-2: GST Reduction in Automobile Industries

The GST reform for health and Nutrition has shown in the following table- 04 and diagram sited below. The given data depicted that except tobacco product for all needy categories of enterprises enjoyed lower GST burden under new GST regime. Keeping view on the health issue the GST has increased for tobacco products radically. It is good sign that the reduction of GST for these micro and small enterprises affect the whole economy positively. Maximum number of peoples especially living in rural areas is engaged with these industries actively and they survive based on these industries activities.

Table- 05: GST reform in Health and Nutrition

Categories	Old GST in percent	New GST in percent	Reform Variation
UHT milk and Paneer	05	Nil	05
Milk based beverages	12	05	08
Dry fruits	12	05	08
Prepared/ preserved Fish	12	05	08
Diabetic foods	12	05	08
Juice based drinks	15	05	10
Tobacco products	28	40	(-12)

Source: Ministry of Micro, Small and Medium Enterprises, 2025

Diagram-3: GST reform in Health and Nutrition

Another important innovation in GST regime has been found in case of textile, leather and housing construction materials. The industries say mam-made fibres, cement, readymade garments, bricks, marbles and granites are example of such industries that enjoyed the benefit of reduced GST. It is quite important to know that the industries are making space for job opportunity for the needy and unskilled labour force. So the reduction of GST, the enterprises gets self-motivations to expand their business. This is another positive issue of new GST regime implemented in India. The given table-5 and corresponding diagram shows the matter clearly.

Table-6: GST Reforms in Textile, leather and Housing Construction Materials

Categories	Old GST in percent	New GST in percent	Reform Variation
Man-made fibres	12	05	08
Leather	12	05	08
Readymade garments	12	05	08
Cement	28	18	10
Bricks	12	05	08
Marbles and granites	12	05	08
Agro-based wood articles	15	05	10

Source: Ministry of Micro, Small and Medium Enterprises, 2025

Diagram-4: GST Reforms in Textile, leather and Housing Construction Materials

The enterprises come under handicraft, logistics, packaging and tourism industries are more vibrant in rural sector. The GST reform hits the progress of such enterprises and they spreading their business rapidly.Tourism is one of the emerging industry where tourism and entrepreneurship working together to develop the tourism sector. Because here maximum employment opportunity may be created. The following table-6 and diagram will picture out the issue evidently.

Table-07: GST Reforms in Handicraft, logistic, packaging, and tourism industries

Categories	Old GST in percent	New GST in percent	Reform Variation
Handicrafts	12	5	08
Toys & Sports goods	12	5	08
Packing papers, cartons etc. logistics goods	12	5	08
Biodegradable bags	18	5	13
Tourism (hotels below Rs. 7500/ day)	12	5	08

Source: Ministry of Micro, Small and Medium Enterprises, 2025

Diagram-5: GST Reforms in Handicraft, logistic, packaging, and tourism industries

Conclusion and policy recommendations

The alteration of tax structure and adoption of GST has been one of the most significant tax reforms in India and its impact on micro, small and medium enterprise appeared as a blessing. On one hand GST has reduced the complexity of multiple taxes, allowed smoother interstate trade and encouraged the business formation over the nation. Maximum benefits comes in medium and large enterprises where micro and small units still continue to struggle with compliance and digital filing requirements. Besides these enterprises also suffering from shortage of working capital. It is true that as MSMEs are working in all regions of the nation these enterprises reduced the regional imbalance. All MSMEs operating as informal sector as established their business at a place where raw materials are available. It is noticeable that under new tax reform where GST has introduced almost all sectors comes under tax reduction target. It has found that keeping GST burden unchanged for large car industries the other automobiles are comes under new GST regime where tax has reduced drastically. GST has reduced in health and nutrition sector, textile industries, construction materials and also in leather products. A remarkable tax reduction observed in handicraft, logistic, packaging, and tourism industries which are very important area of development. The target of new GST reform is to push the MSMEs effectively where maximum labourers can be engaged and the rural people can get benefits of MSMEs from both demand and supply sides.

The following policies can be prescribed to get more return from this new tax regime:

- GST reforms towards reduction of tax rate are good initiatives but the tax implementation procedure should as simple as possible so that micro and small enterprises can advantage of it.
- Proper government monitoring should be there so that both enterprises and government can raise revenue.
- Tax reduction in the form of GST should be higher in case of micro and small enterprises which are working in rural remote areas where maximum needy peoples are engaged with these production units.
- Government should concentrate on handicrafts and tourism sectors where very small enterprises are working but they have significant impact on the rural society.
- To simply the taxation process there should have proper training for the all categories of industries.

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