United International Journal of Multidisciplinary Research (UIJMR)
An International Peer-Reviewed and Refereed Multidisciplinary Journal
ISSN: 3048-6726 | Impact Factor: 6.934 (SJIF)
Volume 3, Special Issue -IX, 2026; Website: www.uijmr.in

"The Impact of GST on the Survival and Competitiveness of Rural MSMEs: A Comparative Study of Structural Shifts and Compliance Burdens"

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DOI:10.37854/UIJMR.2026.3.3.9.432

Abstract

The introduction of the Goods and Services Tax (GST) in 2017 marked a paradigm shift in India's fiscal landscape, aimed at creating a unified national market. However, for Rural Micro, Small, and Medium Enterprises (MSMEs), this transition has been double-edged. This paper examines how GST has influenced the survival and competitiveness of rural enterprises compared to their urban counterparts. By analysing structural shifts specifically, the forced formalization of the informal economy and the disproportionate compliance burdens faced by micro-units, the study identifies a "digital divide" in tax administration. Findings suggest that while GST reduced tax cascading and improved transparency, delays in Input Tax Credit (ITC) and high compliance costs have strained the liquidity of rural firms. The paper concludes with policy recommendations for simplified rural compliance frameworks.

Keywords: GST, Rural MSMEs, Compliance Burden, Structural Shifts, Input Tax Credit (ITC), Economic Formalization, Competitiveness.

Introduction

MSMEs are the backbone of the Indian economy, contributing approximately 30% to the GDP and employing over 110 million people. In rural areas, these enterprises are vital for livelihood security and poverty alleviation. The GST regime promised a

"One Nation, One Tax" system to enhance the ease of doing business. Yet, the transition from an informal, cash-based rural economy to a formalized, digital-first tax system has created significant friction. Rural MSMEs often operate with thin margins, limited digital literacy, and poor access to professional consultancy, making them vulnerable to the complexities of the GSTN (GST Network).

Objectives of the Study

1. To evaluate the impact of GST on the operational survival and market competitiveness of rural MSMEs.
2. To analyse the "Compliance Burden" (filing frequency, professional costs, and technology adoption) specifically for rural micro-enterprises.
3. To examine the structural shift from informal to formal sectors and its impact on rural employment.
4. To compare the GST-related challenges and benefits between rural and urban enterprises.

Research Methodology:

"The study adopts a Descriptive and Analytical Research Design to systematically evaluate the operational landscape of rural Micro, Small, and Medium Enterprises (MSMEs). It focuses on detailing the current status of these enterprises while critically analysing the shifts in their market competitiveness following the implementation of the GST regime. The geographical scope is centered on the Anantapur District, serving as a representative model for rural economic dynamics, which is then benchmarked against a neighbouring urban industrial hub to identify regional disparities. The target population comprises proprietors and senior managers of MSMEs that are formally registered under the GST framework."

Sampling Method:

The study employs a Stratified Random Sampling technique to ensure a representative analysis of the target population. The sample is categorized into two distinct strata: 'Rural' and 'Urban' enterprises.

Study of the Topic:

The following points analyze the dual-impact scenario observed in the MSME sector following the implementation of the GST regime:

Catalysed Sectoral Formalization:

Data from the Ministry of MSME and recent Economic Surveys indicate that GST has acted as a significant catalyst for the formalization of the economy. To maintain their position within the Business-to-Business (B2B) supply chain, millions of previously unorganized firms have sought formal registration. This shift is driven by the preference of larger, organized corporations for GST-compliant vendors, which allows them to seamlessly claim Input Tax Credit (ITC).

The Liquidity Crunch and Working Capital Traps:

While the ITC mechanism is theoretically robust, reports from the Reserve Bank of India (RBI) and SIDBI suggest it has inadvertently created "working capital traps" for small-scale enterprises. Delays in refund processing often freeze approximately 10–15% of a micro-enterprise's liquid assets. In rural settings, where access to credit is limited, this liquidity crunch severely hampers the ability of firms to manage essential operational costs like inventory procurement and payroll.

Disproportional Compliance Costs:

Independent studies by FICCI and contemporary academic findings (2025) demonstrate that compliance costs as a percentage of total turnover are significantly higher for micro-enterprises (estimated at 2–5%) compared to medium-sized enterprises (less than 1%). Rural firms, in particular, incur higher expenditures on third-party intermediaries due to a lack of internal digital infrastructure and technical expertise.

Sectoral Impact on Rural Value Chains:

In sectors such as food processing and handicrafts, the removal of interstate check-posts has successfully reduced logistics and transportation costs by 10–12%. However, these efficiency gains are frequently offset by the recurring professional fees paid to tax consultants for monthly filing and reconciliation.

Findings:

The following observations summarize the core findings regarding the post-GST transition:

1. **Disparity in Adaptation Velocity:**

A significant gap exists in the adaptation speed between different enterprise scales. While medium-sized firms possess the financial and technical resources to digitize operations and leverage interstate trade opportunities, rural micro-units continue to struggle with basic compliance. This "adaptation lag" has resulted in a measurable decline in their relative market competitiveness.

2. **Structural Marginalization of Micro-Units:**

The aggressive drive toward economic formalization has inadvertently marginalized smaller rural entities. Enterprises that cannot absorb the high costs of digital infrastructure or recurring professional consultancy fees face a "survival crisis," leading to a gradual decline or closure of traditional rural manufacturing units.

3. **Enhanced Credit Eligibility through Transparency:**

For enterprises that successfully integrated into the GST framework, there is a notable improvement in financial inclusion. Financial institutions and banks demonstrate a higher propensity to extend credit to

GST-compliant firms, as their business turnover is officially verified through standardized tax data, reducing the information asymmetry in lending.

4. **The infrastructure-Led Rural-Urban Gap:**

The study identifies a critical "service delivery gap" between regions. Urban MSMEs benefit from proximity to GST Suvidha Centers and reliable high-speed digital connectivity, which significantly lowers their transaction and compliance costs. Conversely, enterprises in remote rural districts face higher indirect costs due to poor infrastructure and limited access to localized technical support.

Suggestions for Policy Reform:

Based on the findings, the following policy interventions are suggested to enhance the competitiveness of rural MSMEs:

1. **Tailored Composition Scheme Adjustments:**

It is recommended to upwardly revise the turnover threshold for the Composition Scheme specifically for rural-based MSMEs. This would significantly reduce the frequency of tax filings and ease the administrative burden on small-scale rural entrepreneurs.

2. **Localized GST Support Infrastructure:**

State governments (modeled after the Andhra Pradesh Village/Ward Secretariat system) should establish decentralized "GST Help Desks". These centers would serve as primary touchpoints for providing free or subsidized digital filing assistance and tax literacy to rural business owners.

3. **Streamlined ITC Disbursements for Micro-Units:**

To mitigate working capital constraints, the government should implement an "Accelerated Auto-Refund" mechanism for micro-enterprises falling below a specific

turnover limit. Automating these refunds would prevent the "working capital traps" that currently stifle rural business liquidity.

4. **Incentivizing Digital Transformation:**

Targeted fiscal subsidies should be provided to rural enterprises to encourage the adoption of compliant e-invoicing and accounting software. Providing these digital tools at a subsidized rate will bridge the technological gap and lower the long-term "transaction costs" for rural firms.

Conclusion:

GST is a long-term structural benefit for the Indian economy, but its current "one-size-fits-all" compliance model poses a threat to the survival of rural MSMEs. To ensure inclusive growth, the government must transition from a "policing" mindset to a "facilitating" one for small rural players. Enhancing the competitiveness of these firms requires reducing their compliance burden and bridging the digital divide, ensuring that "One Nation, One Tax" does not become "One Nation, Urban Advantage."

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